THE CENTRAL BANK OF THE RUSSIAN FEDERATION

BANKING SUPERVISION REPORT 2005

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Foreword

The year 2005 was on the whole a good one for the banking sector. Banks expanded their operations significantly and built up their capital. The number and volume of non-cash payments continued to grow, and the payment card market developed dynamically. The establishment of the deposit insurance system was systemically important for the banking sector and now this system is exerting a favourable influence on soundness of Russian banks and promotes confidence of their creditors and depositors. The positive impact of the deposit insurance system is bound to increase as the system develops further.

The main trend in banking sector development in 2005 was the increased competition in virtually all areas of banking, which is undoubtedly a favourable factor of economic development. Competition on the part of international creditors has also increased. The Russian stock market has become more active: corporate bonds may soon become as important a source of financing for some companies as bank loans. Non-bank financial institutions are posting rapid growth. The increased competition is a big challenge for credit institutions, which have to boost their efficiency and learn to operate in a tighter market environment.

It should be noted that rapid growth of the banking sector leads to the accumulation of risks. In this situation it is particularly important to improve the quality of risk management and internal controls in credit institutions. The quality of banking supervision has been subject to more demanding standards.

The Bank of Russia closely monitors the problems involved in banking sector development. *The Banking Supervision Report 2005* deals with these problems and offers their solutions as it analyses the performance of credit institutions, the current state of banking supervision and prospects for its improvement. Also, the *Report* probes some new methods of analysing banking sector stability, including the establishment of a banking sector risk monitoring system, stress testing and the calculation of financial soundness indicators.

I hope this *Report* will give the reader a better idea of patterns of banking sector and banking supervision development in 2005, as well as of the conditions and major factors that affected the Russian banking sector.

Sergey M. Ignatiev,
Chairman of the Bank of Russia

I

The State of the Russian Banking Sector

I.1. General Economic Conditions

I.1.1. Macroeconomic developments

Russia's economy saw rapid growth in major economic activities, household real money income and fixed asset investments in 2005. The output of goods and services increased faster than the official forecast in budget projections for 2005. Consumer prices rose 10.9% over 2005 as against 11.7% in 2004, representing the lowest inflation rate since 1991. The fall in inflation was due to the significant slowing of core inflation, which stood at 8.3% as against 10.5% in 2004. At the same time, the prices of paid services provided to households, including those administered at the regional and municipal levels, and some goods with highly volatile price dynamics continued to increase at rapid rates.

The ruble appreciation against major world currencies was a factor that restrained growth in consumer prices. In 2005, ruble nominal effective rate gained 3.2% against foreign currencies (December 2005 as against December 2004), while the real effective rate rose 10.5% over that period.

The average price of Urals crude rose 45.6% on the world market in 2005 year on year and reached $50.4 per barrel, natural gas prices gained almost 50% on the European market; petroleum product prices were up 40% on average; and there was a rise in the prices of metals and other Russian export commodities. This extremely favourable price situation on world commodity markets for Russian exporters and increased demand for Russian goods led to a massive inflow of foreign exchange to this country and the accumulation of foreign currency reserves, which created conditions not only for the timely servicing and redemption of the government's foreign debt, but also its early repayment.

The balance of payments was characterised by a rise in the current account surplus and international reserves to record highs and a significant inflow of foreign capital to the private sector. The current account surplus increased 40% in 2005 to $84.2 billion, or 11% of GDP ($58.6 billion, or 9.9% of GDP, in 2004). The financial account surplus (net of the change in reserves) stood at $1.2 billion, or 0.2% of GDP (in 2004, Russia had a financial account deficit of $5.5 billion, or 0.9% of GDP).

For the first time capital outflow from the private sector in 2005 equalled inflow (in 2004, net capital outflow from the private sector stood at $8 billion).

The trend towards less household and enterprise sector savings being held in foreign currency continued and in 2005 foreign exchange held by the public on hand decreased by $1.9 billion (in 2004, it declined by $2 billion).

Russia's international reserves expanded almost 50% in 2005 to $182.2 billion, ensuring medium-term financial stability.

GDP increased 6.4% in 2005 year on year as against 7.2% in 2004.

As a result of the improved finances of enterprises and favourable external economic conditions federal budget revenue increased more than expected. The ensuing reduction in non-interest expenditures made it possible to ease inflationary pressure. In 2005, the federal budget surplus stood at 7.5% of GDP as against 4.3% in 2004.

Russia's Stabilisation Fund in 2005 grew faster than expected, allowing the Government to repay ahead of schedule its debt to the International Monetary Fund and a part of the debt it owes to the Paris Club of Creditor Nations.

International rating agencies, such as Standard & Poor's, Fitch Ratings and Moody's Investors Service, raised Russia's ratings to the investment grade in 2005 in recognition of the country's increased solvency and improved investment climate.

I.1.2. The non-financial sector of the economy

The non-financial sector of the economy in 2005 demonstrated continued growth in the production of goods and services in various economic activity categories. As Russia's GDP increased 6.4%, the output index for the basic economic activities registered 106.1%.

Industrial output went up 4.0% in 2005. The output index for the mining industry registered 101.3%. At the same time, growth in the production of fuel and energy stood at 101.8%. Production growth in manufacturing stood at 105.7%. Compared to 2004, there was a fall in the output of machinery and equipment, textile and clothing and leather and leather goods and shoes, largely due to increased competition from imports. At the same time, the output of electrical, electronic and optical equipment rose almost 21.0%. The output index for the production and distribution of electricity, gas and water stood at 101.2%.

The economic activities in which output grew the fastest in 2005 were communications (115.7%), the retail trade (112.0%) and services (107.5%).

Non-financial enterprises pursued their pricing policy in 2005 amid increased state control over prices in the sectors where production was monopolised the most. As a result, industrial producer prices rose 13.4% in 2005 as against 28.8% in 2004.

The development of the non-financial sector was determined not only by the changes in demand and supply on the domestic and foreign raw material and commodity markets, but also the investments made in this sector in 2005. An analysis of data provided by the Federal State Statistics Service shows that until the middle of 2005 growth in fixed capital investment was considerably slower than in the same period of 2004. This negative trend changed in the second half of last year and as a result investment growth in 2005 as a whole remained virtually unchanged from 2004 (110.5% and 110.9% respectively).

Despite slower growth in the output of goods and services in the key economic activities, the overall economic situation remained good and this is additionally evident from the results of the monitoring of enterprises conducted by the Bank of Russia.

According to Bank of Russia surveys of the economic situation in 2005, which covered almost 14,000 enterprises in all Russian regions, the economic conditions began to improve significantly compared to 2004. At the same time, the agricultural enterprises monitored by the Bank of Russia indicated that the economic situation in this activity in 2005 was worse than in 2004.

Owing to favourable economic conditions in 2005, the performance of enterprises in the key economic activities was better last year than in 2004. The Bank of Russia's monitoring showed that the number of enterprises that noted significant improvements in their economic performance increased considerably in 2005. This was particularly applicable to companies in the communications sector, wholesale and retail trade and mining.

The improved economic situation was reflected in the financial results of non-financial sector enterprises.

According to the Federal State Statistics Service, the net financial result, which represents the difference between profit and loss, increased 76.0% in the mining sector in 2005 year on year, 16.2% in the manufacturing sector and 34.0% in the production and distribution of electricity, gas and water.

The net financial result in economic activities such as wholesale and retail trade, as well as repairs, increased 43.0% in 2005 year on year, transport and communications 30.3% and construction 21.1%. At the same time, the net financial result in agriculture, hunting and the forest industry contracted almost 25.0% year on year and fishing and fish farming more than 30.0%.

The Bank of Russia's monitoring indicated that the improved financial position of enterprises in the period under review were due to the improved balance sheet ratios, considerably increased labour productivity and a rise in earnings, which exceeded growth in costs. The improvement of the financial position of enterprises in the period under review was restrained by high bank lending rates, a shortage of own funds for investment and a heavy debt burden carried by most enterprises.

It should be noted here that the financial position of large enterprises (with balance sheets in excess of 1 billion rubles), medium-sized enterprises (with balance sheets in the range of 100 million to 1 billion rubles) and small enterprises (with balance sheets less than 100 million rubles) differed substantially. The financial position of the largest enterprises was relatively good, but other enterprises, especially small ones, had serious financial problems.

The assets of large and medium-sized enterprises increased 10% in 2005. Unlike larger enterprises, small enterprises registered almost a 4% contraction in their balance sheets owing to the decrease in capital assets and net worth. The reduction in small enterprises' capital assets was largely due to the contraction of fixed capital. The net worth of small enterprises, unlike that of large enterprises, decreased by 8%.

Despite the differences in their net worth dynamics, all categories of enterprises registered a slight fall in self-financing. Only the largest enterprises had an adequate level of self-financing from the standpoint of debt coverage in 2005. At the end of last year it stood at 69% of the balance sheet and their debt to net worth ratio was 0.4 rubles. The respective ratios for medium-sized enterprises were 41% and 1.5 rubles and small enterprises 42% and 1.4 rubles.

Enterprises had net-working capital and more opportunities for current asset financing, despite the significant slowing of growth in enterprises' net-working capital. In 2005, the enterprise sector's net-working capital increased 33% as against 62% in 2004.

An analysis of enterprise-sector settlements shows that there was an increase in both the accounts payable and receivable in 2005. At the same time, according to the Federal State Statistics Service, the share of overdue debt in total debt decreased from 11.5% in 2004 to 8.5% in 2005. The share of overdue payables in total payables narrowed to 15.0% as against 18.9% and overdue receivables was down to 13.5% as against 16.2%.

Debts of the enterprises in the mining and manufacturing sectors and the production and distribution of electricity, gas and water account for the largest part of overdue debt payable.

Ninety-four percent of the enterprises monitored by the Bank of Russia said that their demand for the banking services was more or less met. Almost 22% of the enterprises said their demand was met to a great extent and about 6% said their demand was not met. The most significant factors affecting the use of banking services were those connected with enterprises' activities (86% of the interviewed enterprises), confidence in a credit institution (78%), the range of services offered by a credit institution (72%), loan interest rates (70%), document processing procedures (70%) and charges (69%). Fifty-three percent of the interviewed enterprises noted that document processing procedures were typically very complicated and time-consuming.

According to a survey conducted by the Bank of Russia in the fourth quarter of 2005 that covered about 13,000 non-financial enterprises, companies mainly invested to maintain their production capacities. The largest share of such enterprises was in the electric power industry (about 58%). Most of the enterprises that said they invested to expand production were in the fuel sector (over

36%). Most of the enterprises that said they invested to intensify and modernise production were in the ferrous metallurgy sector (57%).

The output of new products was noted as the main purpose of investment by machine-building and metal-working enterprises. Logistics and sales companies noted income as the principal incentive for financial investment, whereas long-term borrowings were the main objective of enterprises in the glass and china enterprises.

I.1.3. Financial markets and non-bank financial institutions[1]

The redistribution of investments from government securities to private sector stocks was the principal trend of the Russian financial market in 2005. The contraction of government debt coincided with unprecedented stock market growth, which was accompanied by the expansion of the ruble corporate bond market. Borrowing on financial markets continued to increase faster than borrowings from banks, although the stock market was still behind the banking sector in investment financing. Borrowings on foreign markets continued to increase.

In the structure of the financial market participants, the banking sector retained its positions of leadership, although assets of non-bank financial institutions grew faster in 2005. Insurance companies developed slower than other non-bank financial institutions. The process of penetration of non-bank financial institutions by banks continued in 2005.

Government debt market. As Russia registered a federal budget surplus and its Stabilisation Fund grew, the country's domestic and foreign debt decreased from 24% to 15% of GDP. Russia repaid ahead of schedule a large part of its debt to the IMF and Paris Club ($18.3 billion). The conservative borrowing policy pursued by the Finance Ministry on the domestic government debt market, the increased demand from the Pension Fund and the high level of excess liquidity in the banking sector led to an excess of demand for federal loan bonds (OFZ) over their supply and, as a consequence, a fall in the average weighted yield.

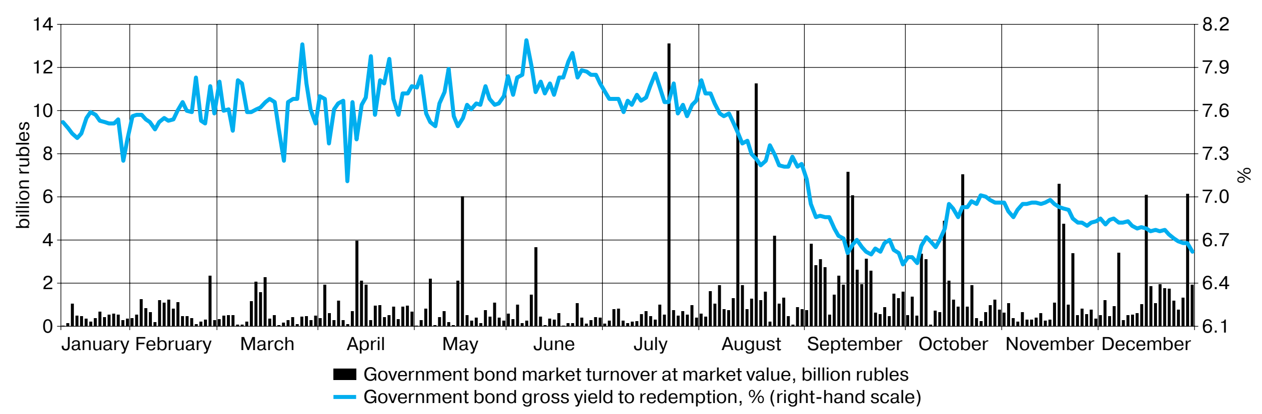
The government securities market's turnover contracted 19%[2] in 2005 year on year, largely as a result of a significant reduction in additional government bond placements on the secondary market. While in January—June 2005 trade volumes were considerably smaller than in the same period of 2004, in the second half of the year the market turnover expanded by more than a quarter as compared with the same period of 2004. Activity peaked in August and September when demand for government securities rose significantly amid expectations of an increase in the price of Russian financial instruments. This was provoked, among other things, by the raising of Russia's sovereign rating and the ratings of some Russian issuers by some agencies, and led to considerable expansion of market turnovers. In addition, the high level of excess liquidity, especially the balances in correspondent accounts with the Bank of Russia, stimulated growth in the demand for government bonds.

There were two periods in government securities yield dynamics in 2005: in the first half of the year interest rates were most as high as 7.4—8.0%, whereas in the second half rates tended to decline as demand for domestic government debt instruments rose. As a result, by the end of the year the gross yield to redemption of government securities fell to 6.6% *(see Chart 1.1).*

Market liquidity remains at a low level. The government securities market could have attracted more investors if yields had been higher and the market had had more diverse participants (passive investors predominate).

The role of the banking system in this segment of the market is gradually declining, although it remains quite important. By the end of 2005, the banking sector's share of the ruble-denominated government bond market contracted to almost 50% from 55% a year earlier. At the same time, banks became increasingly interested in su-

Government securities market turnovers and yields in 2005 *CHART 1.1*



[1] Materials provided by the Economic Research Foundation Development Centre were used in compiling this subsection.
[2] Excluding operations that have non-market characteristics due to the specific accounting policy adopted by some big investors.

per-long-dated bonds as a speculative investment. As the funded pension system gains ground, the role of the Pension Fund is increasing on the ruble-denominated government bond market. The non-resident share of the OFZ bond market was extremely small in 2005 (0.2%).

The upgrading of Russia's credit rating and the positive external economic situation reduced yields on Russian *foreign currency-denominated government securities.* Non-residents play a key role on the Russian foreign currency bond market, accounting for more than two thirds of its volume. Russian investors account for about 28% of this market, of which the share of commercial banks stands at nearly 10%. The share of non-bank financial institutions was 8% at the end of 2005.

Corporate securities markets. Last year was extremely successful for the Russian *stock market.* As a result of high oil prices and favourable macroeconomic dynamics, the RTS index gained 83.3% and reached 1,125.6 points *(see Chart 1.2).* RTS trade turnovers expanded by a third.

As a result of the stock market's expansion, the capitalisation of the Russian companies in the RTS increased to $330 billion. The Russian market became the world's fourth most attractive market for investment (after Brazil, India and China) and non-resident activity rose and trade turnovers expanded as a result.

The decline of the banking sector's share of the stock market (to 5%)[3] and growth in non-resident and non-bank financial institution investments indicate that the structure of investors has changed.

The expansion of the corporate bond market accelerated in 2005. The volume of the ruble bond market expanded 80% in nominal terms and reached two-thirds of the domestic government debt market volume.

High demand for new ruble-denominated instruments amid the decline in OFZ bond yields led to the reduction of effective yields on the corporate bond market. The effective yield of the RUX-Cbonds index[4] fell from 9.3% p.a. to 7.0% p.a. in 2005. The declining cost of borrowing and the appreciating ruble encouraged enterprises to place new bond loans.

Competition continued to increase between bond loans and bank lending. The corporate bond market grew 2.7 times faster than the loan portfolio of Russian banks, as the average lending rates remained virtually unchanged in 2005, while bond loan rates declined. As a result, the volume of the ruble bond market in 2005 reached 16.5% of the volume of ruble loans extended by banks to the enterprise sector and 11.5% of total loans to this sector (a year earlier, the respective percentages were 11.8% and 8.3%).

Long-term bank lending and bond borrowing continued to expand. Long-term bank loans extended to the enterprise sector in rubles increased 65% in 2005, and loans with maturities over three years grew 120%, or 1.5 times faster than market corporate borrowings. Average weighted interest rates on ruble loans to the enterprise sector with maturities over three years were comparable with market rates on bond loans.

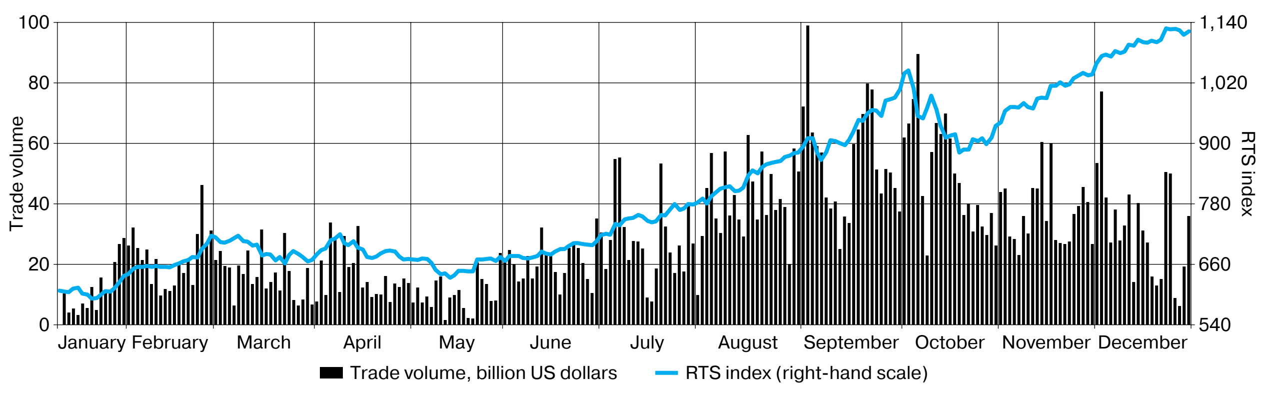
The share of the banking sector as an investor on the corporate bond market in 2005 expanded from 49.0% to 52.2%. In addition, banks were proactive on the corporate bond market as loan arrangers.

Russian companies' borrowings on international financial markets continued to grow faster than domestic bank lending in 2005. Eurobond growth twice surpassed growth in lending volumes. The corporate eurobond market expanded 64.5% in 2005, according to Cbonds data, and the number of outstanding issues increased 82.0%. The range of borrowings became considerably diversified.

In 2005, Russian banks placed more than half of all issues and their share in the total volume of outstanding eurobonds issued by Russian companies reached 44%.

RTS Index Dynamics in 2005

CHART 1.2



Source: RTS, Development Centre's calculations.

[3] It should be remembered, however, that banks also often operate on this market through affiliated management companies or general bank management funds (OFBU).
[4] Bonds issued by the most secure issuers are included in the calculation of the index. Depending on the issuer, bond yields are in the range of from 6% to 14% p.a.

Domestic foreign exchange market. The situation on the domestic foreign exchange market in 2005 was affected by a massive inflow of foreign currency to the economy as a result of unprecedented revenues from exports due to the high prices of major export commodities and continued active borrowings by Russian companies abroad. The increased current account surplus, which was not offset by corresponding capital outflow, ensured that supply of foreign currency far outstripped demand. Bank of Russia operations, conducted in line with its monetary policy, US dollar dynamics on the world market and credit institutions' actions with regard to their open positions in foreign currency played a key role in shaping the situation on the domestic foreign exchange market. The foreign exchange market remained the most important and liquid segment of the financial market: conversion operations' volumes far outstripped turnovers on the interbank and stock markets.

For most of 2005, the US dollar was strong against the euro on the world foreign exchange market, causing its rate against the ruble to rise on the domestic market. Overall, the US dollar appreciated 3.7% against the ruble in nominal terms.

Growth in exports and imports and capital flow dynamics determined the high level of market participants' activity in buying and selling foreign exchange. As a result, the average daily turnover of interbank spot market expanded 28% in 2005 year on year.

Ruble/US dollar transactions predominated in the currency structure of the interbank segment of the market, accounting for more than two-thirds of the total turnover. At the same time, as market participants became increasingly interested in the single European currency, the euro trade turnover expanded, mainly due to the euro/US dollar transactions, which accounted on average for over 90% of the total euro transaction volume. Overall, the volume of spot interbank operations with the euro expanded 29% in 2005, whereas the volumes of operations with other currencies remained negligent.

The Single Trading Session (STS) of interbank currency exchanges retained its role as a segment of the domestic foreign exchange market where the rate setting process is the most transparent and reflects the current balance of foreign trade operations and capital flows.

There was a rise in exchange trade participants' activity in 2005: total STS ruble/US dollar trade volume grew 69% year on year and ruble/US dollar "tomorrow" trades accounted for most of the turnover (44%). Ruble/US dollar "today" trades accounted for 28% of total STS ruble/US dollar trade volume and currency swaps 28%. Although the aggregate STS ruble/euro trade volume expanded 83% in 2005 year on year, ruble/euro transactions in both the exchange and over-the-counter segments of the domestic foreign currency market accounted for only about 1% of the total volume of transactions with the Russian ruble.

Overall, the exchange segment's share in the interbank market total turnover expanded to nearly 12.8% in 2005 (net of over-the-counter transactions) as against 9.1% in 2004.

Spot operations accounted for the largest part of transactions (over 95%) in the exchange and over-the-counter segment of the interbank foreign currency market. The low level of activity in the derivatives segment of the market was largely due to a lack of effective legal protection for market participants conducting operations with its instruments.

The role of non-bank financial institutions in the Russian financial system[5]

Insurance companies. The insurance sector consolidated and insurance companies continued to abandon tax optimisation schemes in 2005. As a result, the number of insurance companies has fallen by 25% over the past three years. The measures taken by the Federal Insurance Supervision Service were the main reason for the decrease. Some insurance companies had their licences revoked for using illegal life insurance schemes that allowed enterprises to pay lower taxes. More stringent minimum authorised capital requirements have been imposed on insurance companies and measures have been taken to prevent the use of improper assets for capital padding. In addition, new rules on the placement of insurance reserves were introduced in 2005.

As of the middle of 2005, the insurance companies' aggregate assets accounted for 7.5% of aggregate banking sector assets and capital for nearly 17% of aggregate banking sector capital *(see Table 1.1).*

The insurance market grew slower than other non-bank financial institutions over 2005 mainly because of the sharp reduction of life insurance premiums and the revocation of licences from several large companies. At the same time, premium dynamics in other categories of voluntary insurance were positive: life and property insurance premiums rose 20% and liability insurance premiums increased more than 30%.

In the compulsory insurance segment, insurance indemnities grew faster than premiums. In 2005, compulsory insurance indemnities rose 40.8%, whereas premiums increased by just 32%. The difference was particularly striking in the compulsory third party liability auto insurance segment, where indemnities increased 43.5% and premiums 9.1%. Overall, the share of compulsory insurance, except life insurance, has been expanding in insurance premiums: in 2005, it stood at 54.2% as against 46.3% in 2004.

The reduction of voluntary insurance indemnities amid growth in compulsory insurance indemnities led to a sharp increase in the share of compulsory insurance in total insurance indemnities (from 38% to 60%). As a result, compulsory insurance operations became even less profitable.

[5] Unless stipulated otherwise, non-bank financial institutions are insurance companies, management companies (MCs) and non-government pension funds (NPFs).

In terms of concentration levels, the insurance sector is similar to the banking sector. The top 50 companies dominate the insurance market, controlling from 50% to 80% of its various segments. State-owned companies are the market leaders. The top five insurance companies account for 21.6% of total insurance premiums and the top 50 companies about 60%.

Insurance companies invest from 40% to 50% of their assets. Overall, the structure of insurance companies' financial investments is stable. Insurance companies invest more than half of their funds in corporate sector financial instruments, which make their investment portfolios riskier than those of banks. At the same time, the share of government securities expanded slightly in the insurance companies' portfolios (from 3.4% in the middle of 2004 to 7.3% in the middle of 2005). Insurance companies keep a large part of their investments (about 17%) in bank deposits, accounting for about 6% of corporate sector time deposits with banks. The insurance companies' share of the corporate securities market is estimated at 5—6% (as compared with the banking sector's share of 22%) and insurance companies account for 1—2% of the government bond market (as compared with the banking sector's 30%).

Last year was good for Russia's *collective investment institutions.* The improved economic situation in the country along with growth in household income, reduced interest rates on bank deposits and good performance indicators of management companies for 2004 stimulated the inflow of funds to various collective investment institutions. However, all collective investments account for only 18% of household deposits with commercial banks (as against 14% as of the beginning of 2005), although deposits grew slower than the assets of collective investors.

Unit investment funds (PIFs). PIFs were the most dynamic institutions on the collective investment market in 2005. The number of PIFs increased 50% year on year and management companies 30%.

Stock funds account for most of the investments (51% of the total net asset value of all unit funds), although in 2005 the stock funds' share contracted 4%.

The top 10 management companies account for about 75% of total net assets and the share of the management companies connected with commercial banks is about 24%.

General bank management funds (OFBU). Last year was more successful for OFBU than PIFs from the standpoint of performance indicator dynamics, although in absolute terms OFBU assets are considerably smaller than those of PIFs.

The OFBU number more than doubled in 2005 and the value of their net assets almost tripled. The rates of return of the OFBU investing on the Russian market ranged from 13% to 82% p.a., depending on the strategy (stock funds were the most profitable). The rates of return of the foreign currency OFBU differed even more: from —30% to 120% p.a. At the same time, OFBU offered their shareholders a wider range of instruments. However, total risk of the OFBU portfolios is higher than that of PIFs.

The top 10 OFBU account for almost 98% of the market. This high level of market concentration highlights the market's underdevelopment and inadequate diversification.

Non-government pension funds (NPFs). Pension reserves increased from 170 billion rubles to 277 billion rubles in 2005, while the value of the NPFs' own property rose from 216 billion rubles to 344 billion rubles. At the same time, the number of NPFs declined from 271 to 261, mostly due to mergers.

The top 10 NPFs account for 87% of pension savings. The number of NPFs affiliated with banks is relatively small and the ratio of the reserves they accumulated to the assets of these banks is negligent.

About 10% of all pension reserves are invested in bank deposits. In addition, NPFs buy bank securities, especially promissory notes, which account for about 4% of NPFs' total investments.

Banks continued to infiltrate non-bank financial institutions in 2005. Of the top 50 Russian banks, 31 were members of various associations or had non-financial subsidiaries at the beginning of this year. Financial groups with a wide range of businesses are developing the most dynamically. Banks and non-bank financial institutions have equal shares in terms of assets and capital in some of them. Such a group operates like a financial supermarket[6]. However, the assets of banks and non-bank finan-

Banking sector assets to non-bank financial institutions' assets as of beginning of 2006

TABLE 1.1

	No. of institutions	Assets, billion rubles	Assets relative to GDP (%)	Growth in assets over year (% of GDP)	Share in financial institutions' assets	Change of share over year (percentage points)
Banking sector	1,253	9,750.3	45.0	3.0	89.3	—0.9
Insurance companies	1,075	585.0	2.7	0.1	5.4	—0.3
Non-government pension funds	261	344.0	1.6	0.3	3.2	0.5
Unit investment funds	360	228.2	1.1	0.5	2.1	0.8
Total	2,949	10,907.5	50.4	3.9	100.0	

Source: Bank of Russia, Federal Insurance Supervision Service, Federal Financial Markets Service and Development Centre's estimates.

[6] Selling the entire range of financial services under one roof.

cial institutions are still incomparable and the financial system's stability largely depends on the state of the banking sector.

I.1.4. Payment system

The state of the Russian payment system in 2005 helped maintain financial stability in the country and the Bank of Russia's implementation of the monetary policy and creating conditions for increased business activity.

The Russian payment system effected 1,116.8 million payments to the amount of 293.5 trillion rubles in 2005. The value of payment rose 31.1% in 2005 as against 22.9% in 2004; the number of payments increased 12.6%, which represents a decrease from the previous year's 16.0%.

The Bank of Russia payment system in 2005, as in the past, dominated the Russian payment system in terms of both the number and value of payments. Payments effected by the Bank of Russia payment system accounted for 49.8% of total payments effected by the Russian payment system and 66.1% of the total value of payments (the respective percentages in 2004 were 47.6% and 60.5%).

The number and value of payments effected by the Bank of Russia payment system continued to increase in 2005: 555.6 million payments to the amount of 194.0 trillion rubles were effected. The number of payments increased 17.7% year on year and in value they grew 43.3% (the respective growth rates for 2004 were 14.6% and 25.1%). The average daily number of payments rose 15.8% to 2.2 million.

Growth in the number and value of payments was due to the attractiveness of the Bank of Russia payment system, which is the least risky for participants, and the Bank of Russia's constant work to upgrade its payment system and make it efficient and fail-safe.

The Russian payment system continued to increasingly use electronic payments, which accounted for 84.0% of the total number of payments and 91.9% of their total value (77.5% and 86.8% in 2004).

The Bank of Russia monitored the payment system and upgraded the system of indicators characterising its state and development.

In 2005, it inspected the security of its payment system by using a series of indicators designed for analysing the accessibility of the Bank of Russia payment system, i.e., its readiness to accept settlement documents electronically and on paper from clients. These indicators showed that the Bank of Russia payment system was stable from the standpoint of accessibility. The average monthly accessibility ratios were in the range of 99.79% to 99.95% in terms of the acceptance by the Bank of Russia of electronic documents from its clients and 99.99% to 100% in respect to settlement documents on paper.

To implement the Russian Banking Sector Development Strategy until 2008, which sets out the establishment of a real-time gross settlement system (RTGS) by the Bank of Russia, the latter in 2005 carried out a series of measures to accomplish this objective.

Specifically, the Bank of Russia set up the RTGS Development Committee, which drafted a document entitled "Functional Requirements for the Bank of Russia RTGS". This document laid down the main principles of developing and operating the RTGS, contained higher-level description of the main elements of the system and its structure, set requirements for the participants in the system and the functions it should fulfil and established the procedure for effecting payments. The working groups formed within the framework of the Committee analysed legal and regulatory framework with the objective of making the necessary amendments to it in line with the RTGS and drafting new regulations. They also prepared the corresponding proposals.

The establishment of the RTGS will help reduce settlement risks that arise in the payment system in effecting large payments, increase financial stability, make the monetary policy more effective and create conditions for integration with international payment systems.

In 2005, the Bank of Russia continued to work on a new draft of its Regulation on Non-cash Settlements in the Russian Federation, which systematises the rules on non-cash settlement instruments, procedures and forms and specifies the effectuation of non-cash settlements within various payment systems. The draft standardises the requirements for the non-cash settlement procedure regardless of the processing and transmission of non-cash settlement orders (using electronic and paper documents, payment cards and electronic means of payment). As the document avoids describing banking procedures in great detail, banks will be able to take a more flexible approach to the development and introduction of new payment services.

A well-considered legal and regulatory framework pertaining to the payment system is essential for its stability. It helps increase confidence in the banking system and, as a consequence, stimulate demand for settlement services by corporate entities and private individuals in the country's regions.

The number of accounts opened to clients with the Bank of Russia and credit institutions and their branches for effecting payments continued to increase: the number of such accounts rose 12.2% to 353.5 million as of January 1, 2006, of which 1.4% were accounts opened by corporate entities other than credit institutions and 98.6% the accounts opened by private individuals.

The coming into force on April 10, 2005, of Bank of Russia Regulation of December 24, 2004, No. 266-P "On the Issue of Bank Cards and Payment Card Operations", facilitated the further expansion of the payment card market.

The number of payment cards increased 55.5% in 2005 (46.4% in 2004). Payments effected with payment cards continued to increase rapidly: by 41.4% in number and 43.5% in value (48.5% and 68.3% in 2004). The range of services provided by credit institutions and their branches using payment cards and the infrastructure accepting payment card continued to expand (over the year, the number of trading and service establishments accepting bank cards and ATMs used for paying for services increased 34.9% to 142,500).

The credit card market grew faster in 2005. In terms of card numbers it increased 87.9%, in terms of credit card operations 88.7% and in terms of the value of operations 110.9%. However, despite this rapid growth, credit card operations accounted for a lowly 1.6% of total payment card operations.

Non-cash payments effected using payment cards accounted for 16.7% in 2005 as against 15.6% in 2004 and, as in the previous years, cash withdrawal operations exceeded non-cash payments (83.3% in numbers and 89.4% in value).

I.1.5. Banking sector performance indicators relative to key macroindicators

Banking sector assets increased 36.6% in 2005 as against 27.4% in 2004. Banking sector own funds (capital) expanded 31.2% over that period as against 16.2% in 2004. Loans extended to non-financial corporations and households increased 40.3% as against 44.8% in 2004, while household deposits grew 39.3% in value as against 30.3% in 2004.

As a result, the ratio between these indicators and GDP increased. The ratio of banking sector assets to GDP rose by 3.1 percentage points to 45.1%; the ratio of banking sector own funds (capital) to GDP stood at 5.7%, virtually unchanged from 2004 (5.6%); the ratio of household deposits to GDP increased by 1.1 percentage points to 12.8%; the ratio of loans to non-financial corporations and households (individuals) expanded by 2.3 percentage points to 25.3%.

Lending was the main source of growth in banking sector assets in 2005, as was the case a year earlier. Loans to the real sector of the national economy (resident non-financial corporations) increased 30.5% as against 39.0% in 2004 and its ratio to GDP expanded by half a percentage point to 19.0%, whereas its share in aggregate banking sector assets stood at 42.2% as against 44.1% in 2004. Loans to households (individuals) increased 90.6% as against 106.5% in 2004 and its ratio to GDP grew by 1.8 percentage points to 5.5% and its share in aggregate banking sector assets expanded by 3.4 percentage points to 12.1%.

The main source of resources for credit institutions in 2005 was corporate funds, which increased 48.7% as against 43.4% in 2004. Their ratio to GDP expanded by 2.0 percentage points to 13.7% and their share in banking sector liabilities rose by 2.5 percentage points to 30.3%.

The positive dynamics of the key banking sector performance indicators amid their increased ratio to GDP show that the banking sector is continuing to play a greater role in the Russian economy.

I.2. Institutional Aspect of Banking Sector Development

I.2.1. Banking sector quantitative characteristics

The number of credit institutions decreased from 1,299 to 1,253 in 2005 *(see Chart 1.3).* Forty credit institutions, including two in the top 200 in terms of assets, had their licences revoked last year; 14 credit institutions were struck off the State Register of Credit Institutions as a result of mergers and acquisitions and eight new ones came into operation. The number of credit institutions declined for the straight second year: while in 2001—2003 the number of operating credit institutions rose slightly, in 2004—2005 their number fell by 76.

The establishment of the deposit insurance system was a major contributing factor. The selection of banks for participation in the deposit insurance system had been largely completed in 2005, as required by law. As of January 1, 2006, 931 banks were registered as members of the system, which represents 74% of the total number of credit institutions operating in Russia, and these banks account for almost 99% of all household accounts.

As of January 1, 2006:

— 1,045 credit institutions, or 83.4% of the total number of operating credit institutions have the right to take household funds on deposit (as against 1,165 credit institutions, or 89.7% of the total, as of January 1, 2005, and 89.5% as of January 1, 2004);

— 827 credit institutions, or 66% of the total, have the right to conduct banking operations in rubles and foreign currency (as against 839 credit institutions, or 64.6% of the total, as of January 1, 2005, and 63.6% as of the beginning of 2004);

— 301 banks, or 24% of the total, have a general licence to conduct banking operations (as against 311 banks, or 23.9% of the total, as of January 1, 2005, and 23.3% as of January 1, 2004);

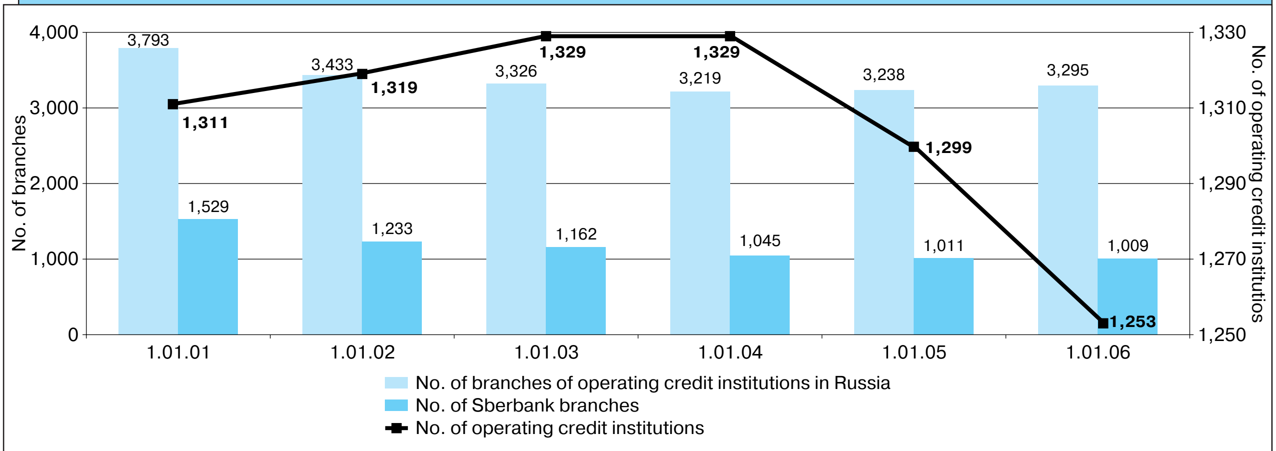
— 184 credit institutions, or 14.7% of the total, have the right to conduct operations with precious metals under licence to take precious metals on deposit and to invest them as well as permits to conduct operations with precious metals (as against 182 credit institutions, or 14% of the total, as of January 1, 2005, and 13.6% as of January 1, 2004).

The number of credit institutions declined almost in all federal districts, including Moscow and the Moscow Region, where the number of credit institutions fell by 25 over the year. The only exception was the Far Eastern Federal District, where the number of local credit institutions remained unchanged during the year and was smaller than in any other federal district (43).

Credit institutions continued to reorganise their branch network during the year under review. Over the year, the number of branches of credit institutions increased slightly and as of January 1, 2006, stood at 3,295 as against 3,238 as of January 1, 2005, an increase of 1.76% or 2.36% as compared with January 1, 2004. Of the total number of credit institutions' branches in Russia, 1,009 were Sberbank branches as of January 1, 2006. As compared with January 1, 2005, their number fell by two.

In 2005, credit institutions and their branches continued to increase the number of internal divisions, such as additional offices and cash credit offices. At the same time, there was a fall (from 18,491 to 17,662) in the total number of cash points. The total number of internal divi-

Number of credit institutions and their branches CHART 1.3



sions of credit institutions and their branches increased by 1,964 over the year and stood at 29,634 as of January 1, 2006, as against 27,670 as of January 1, 2005.

In all federal districts, except the Central Federal District, the number of branches of banks based in other regions exceeded the number of local credit institutions and their branches as of January 1, 2006. A year earlier, local credit institutions and their branches also predominated in the Ural Federal District.

I.2.2. Banking sector development at the regional level[7]

The number of regional banks[8] fell slightly in 2005: from 628 as of January 1, 2005, to 607 as of January 1, 2006. Growth in the regional banks' assets in 2005 (by 32.2%) was slower than that in aggregate banking sector assets (by 36.6%). As a result, the share of the regional banks in aggregate banking sector assets contracted slightly and as of January 1, 2006, it stood at 15.0% as against 15.5% as of January 1, 2005.

The aggregate own funds (capital) of the regional banks increased by 30.2 billion rubles, or 18.7%, in 2005, but its share in aggregate banking sector own funds (capital) contracted to 15.4% from 17.0% as of January 1, 2005.

Regional banks remained profitable in 2005. They posted a profit of 34.1 billion rubles, an increase of 29.0% on 2004. The share of profit-making regional banks in total regional banks expanded by one percentage point over the year to 99.3% as of January 1, 2006, and the share of profit-making regional banks in regional banks' total assets stood at 99.9%.

The region with the best supply of banking services[9] in 2005 was the North-Western Federal District, which improved its leading position over the year due to the most rapid rates of growth in assets and household deposits. The aggregate level of supply with banking services in the Volga Federal District and Central Federal District was also above the national average.

The Ural Federal District had the worst supply of banking services in 2005, replacing the traditionally far behind Siberian Federal District because it had the smallest ratios of assets and loans to regional GDP. The supply of banking services in the Southern Federal District and Far Eastern Federal District was also below the national average.

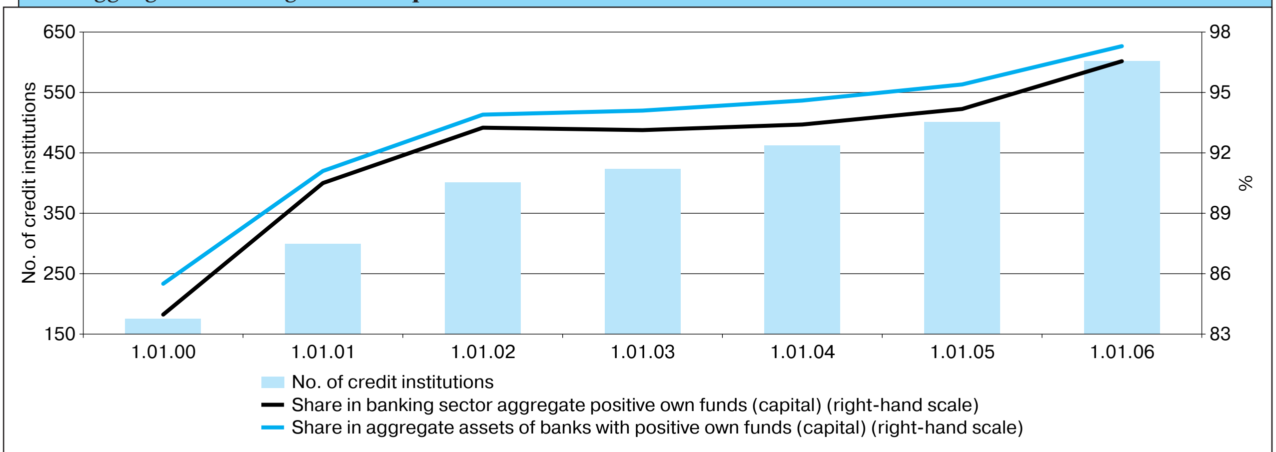
The worst supply of banking services among the constituent members of the Russian Federation was registered, as in the past, in the Republics of Ingushetia and Daghestan; the best was in St Petersburg, the Magadan and Kaliningrad Regions.

As of the beginning of 2006, there were not more than two operating local credit institutions in 14 constituent members[10] (the Bryansk, Kursk, Lipetsk, Novgorod, Orel, Penza, Tambov and Chita Regions and the Republics of Buryatia, Ingushetia, Kalmykia, Karelia, Tyva and Marii El)[11]. In three constituent members of the Russian Federation (the Jewish Autonomous Region, Chukchee Autonomous Area and Chechen Republic) there were no operating credit institutions as of January 1, 2006, as was the case in previous years.

I.2.3. Banking sector concentration levels

The share of the **200** largest credit institutions in terms of assets in aggregate banking sector assets re-

Number of banks with own funds (capital) in excess of €5m and their share in aggregate banking sector capital *CHART 1.4*



[7] Regional banks are those registered outside Moscow and the Moscow Region.
[8] Data on the number of regional banks are cited regardless of their assets. In *1.2.4 Banking sector clustering* these banks are clustered, including by assets.
[9] The level of supply with banking services was calculated without taking into account credit institutions based in Moscow and the Moscow Region.
[10] Not counting the autonomous areas within other constituent members of the Russian Federation.
[11] As of January 1, 2006, this group of constituent members included the Republic of Tyva, where the number of operating local credit institutions declined from three to two in 2005.

mained virtually unchanged in 2005 and as of January 1, 2006, it stood at 89.6% as against 89.0% as of January 1, 2005, but the share of the top **five** banks contracted from 45.1% to 43.8%.

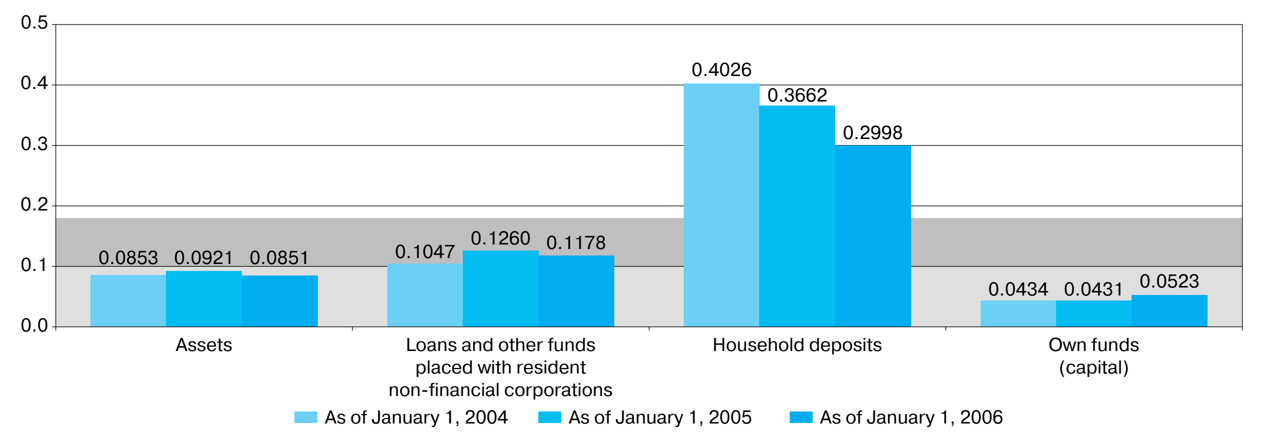
The **200** largest credit institutions in terms of own funds (capital) accounted for 85.1% of aggregate banking sector own funds (capital) as of January 1, 2006, as against 82.9% as of January 1, 2005, of which the top **five** banks accounted for 36.0% as against 34.0% as of January 1, 2005.

The number of credit institutions with own funds (capital) in excess of €**5** million increased from 501 to 602, or by 20.2%, in 2005 (the aggregate own funds (capital) of this group of banks grew 34.5%) and their share in aggregate banking sector own funds (capital) expanded from 94.0% to 97.0% *(see Chart 1.4)*. The number of credit institutions with own funds (capital) of more than €**5** million reached almost 50.0% of the total number of credit institutions (48.0% as of the beginning of 2006 as against 38.6% a year earlier) and this year the number of credit institutions with own funds (capital) of over €**5** million will exceed, by estimates, the number of institutions that do not meet this criterion.

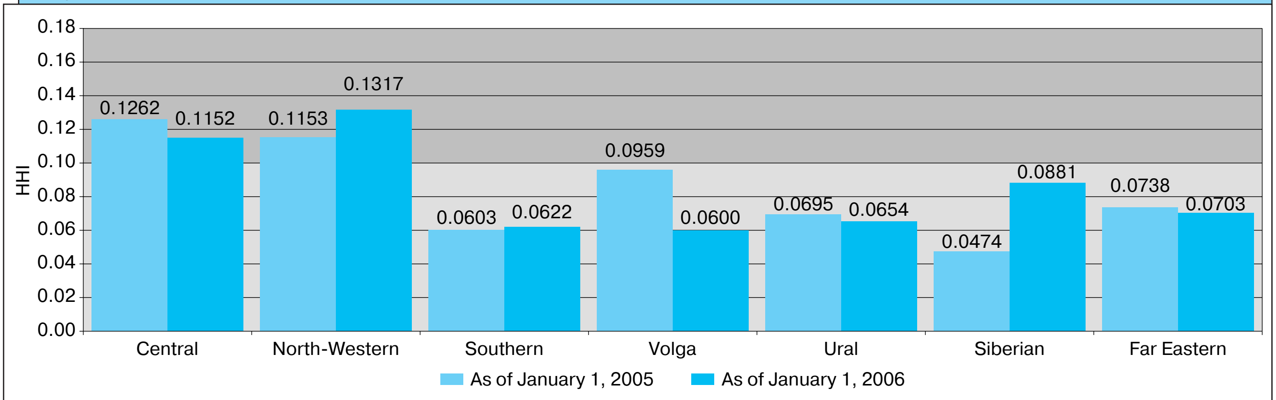
At the same time, the Russian banking sector has a low level of asset, loan and capital concentration because it comprises a considerable number of medium-sized and small credit institutions (with own funds (capital) of less than €**5** million). The dynamics of the internationally-accepted Herfindahl-Hirschman Index (HHI)[12] bear this out *(see Chart 1.5)*. After a slight rise in 2004, the index of concentration of assets returned to the low level registered in early 2004. Similar dynamics were observed in the level of concentration of loans to the sector of non-financial corporations: after a minor increase in 2004, it fell to 0.118 in 2005. Thus, the concentration level of loans to the sector of non-financial corporations in 2005 may be described as medium.

Only the household deposit market had a high concentration level, despite sustained downward dynamics. As of January 1, 2006, the HHI of this market segment

Russian banking sector concentration levels (HHI) *CHART 1.5*



Asset concentration by federal district *CHART 1.6*



[12] The Herfindahl-Hirschman Index is recommended by the Compilation Guide on Financial Soundness Indicators drafted by the IMF as a measure of concentration in the banking sector. It is calculated as a sum of squared unit weights of a credit institutions' indicator in the total volume of the banking sector indicator. The Index shows the extent of the indicator's concentration on the scale of values from 0 to 1. The value 0 signifies the lowest level of concentration, less than 0.10 a low level of concentration, 0.10 to 0.18 a medium level of concentration and more than 0.18 a high level of concentration.

Performance indicators of credit institutions' groups*

TABLE 1.2

Credit institutions' groups	Number	% share in aggregate banking sector assets	% share in aggregate banking sector own funds (capital)
State-controlled banks	32	40.7	33.8
Banks controlled by foreign capital	51	8.3	9.2
"Intra-group" banks	109	16.2	19.4
"Diversified" banks	74	25.1	23.4
Medium-sized and small banks based in the Moscow Region	455	5.1	8.6
Regional medium-sized and small banks	484	4.2	5.4
Non-bank credit institutions	48	0.5	0.2
TOTAL:	1,253	100	100

** Clustering criteria and performance indicators of above credit institutions' groups are used solely for analysis in this work.*

registered 0.30 as against 0.46 three years earlier. The significant decline of the index over the past few years was largely due to the contraction of Sberbank's share of the household deposit market. This was because of tough competition for household savings, which had increased after the enactment of Federal Law of December 23, 2003, No. 177-FZ "On Insurance of Household Deposits with Banks of the Russian Federation" and the establishment of the deposit insurance system.

The capital concentration level is the lowest banking sector performance indicator (0.052), although in 2005 it rose slightly after several years of continuous decline.

Significant regional differences in concentration levels remained on the banking services market in 2005 *(see Chart 1.6).*

The highest bank asset concentration level (HHI stood at 0.13) was registered in the North-Western Federal District, which for the first time took the lead over the Central Federal District in this respect. The concentration levels in these two federal districts are regarded as medium. The other federal districts have low concentration levels. It should be noted that while in 2004 the lowest asset concentration level was registered in the Siberian federal district, subsequently the asset concentration level in this federal district almost doubled (higher growth than in any other federal district) and it rose to the third place after the North-Western and Central Federal Districts. Apart from the North-Western and Siberian Federal Districts, a slight rise in the asset concentration level was registered in the Southern Federal District, whereas all other federal districts posted a fall in these levels in 2005.

I.2.4. Banking sector clustering

There are various groups of banks in the Russian banking sector, which differ by development strategy, risk profile, clientele and sources of funds. To analyse the banking sector, the Bank of Russia has clustered credit institutions on the basis of a combination of several characteristics.

The clustering of the banking sector, conducted as of January 1, 2006 *(see Table 1.2),* showed that state-controlled banks accounted for the largest share in assets (40.7%) and own funds (capital) (33.8%). The third and second largest groups comprised "intra-group" and "diversified" banks[13], whose aggregate share in assets and own funds (capital) is comparable with that of the state-controlled banks.

Banks controlled by foreign capital accounted for 8.3% of banking sector assets and 9.2% of banking sector own funds (capital). The rise in the activity of this group of banks in 2005 provides grounds to believe that their share in aggregate banking sector assets and own funds (capital) will continue to expand.

The largest groups comprise regional medium-sized and small banks and medium-sized and small banks based in the Moscow Region, but their share in aggregate banking sector assets is small (4.2% and 5.1% respectively).

[13] "Intra-group" banks are those controlled by one or several related owners and determined as such by expert judgement, which is passed if a person or a group of related persons has a 50%-plus stake in a credit institution or if there is a persistently high level of large credit claims per borrower or if there is evidence of preferential lending to related borrowers. "Diversified" banks are the largest banks other than those controlled by the state or foreign capital and not intra-group. The principles of clustering the banking sector are set out in detail in *Annex IV.4.*

I.3. Banking Operations

The main trend in banking sector development in 2005 was the increased competition in all banking activities. The intense competition from international creditors on the Russian money and capital market could be seen, among other things, by the increased number of potential sources for financing the non-financial sector of the economy. These are larger borrowings from foreign banks, eurobond placements by companies and the issue of depository receipts. Mention should also be made of the rapid expansion of the ruble bond market.

Foreign capital is rapidly building up its presence in Russia. The number of foreign-controlled credit institutions in the Russian banking sector reached 52 as of January 1, 2006, as against 42 as of January 1, 2004, of which nine are among the top 50 banks by assets operating in Russia. The assets of the foreign-controlled banks increased 49.3% in 2005 and their own funds (capital) expanded 56.4%. As a result, the share of the foreign-controlled banks in aggregate banking sector assets expanded from 7.6% as of January 1, 2005, to 8.3% as of January 1, 2006 and in own funds (capital) from 7.8% to 9.3%.

I.3.1. The dynamics and structure of borrowed funds

The resource base of credit institutions continued to expand in 2005 amid structural changes in banking sector liabilities *(see Chart 1.7).*

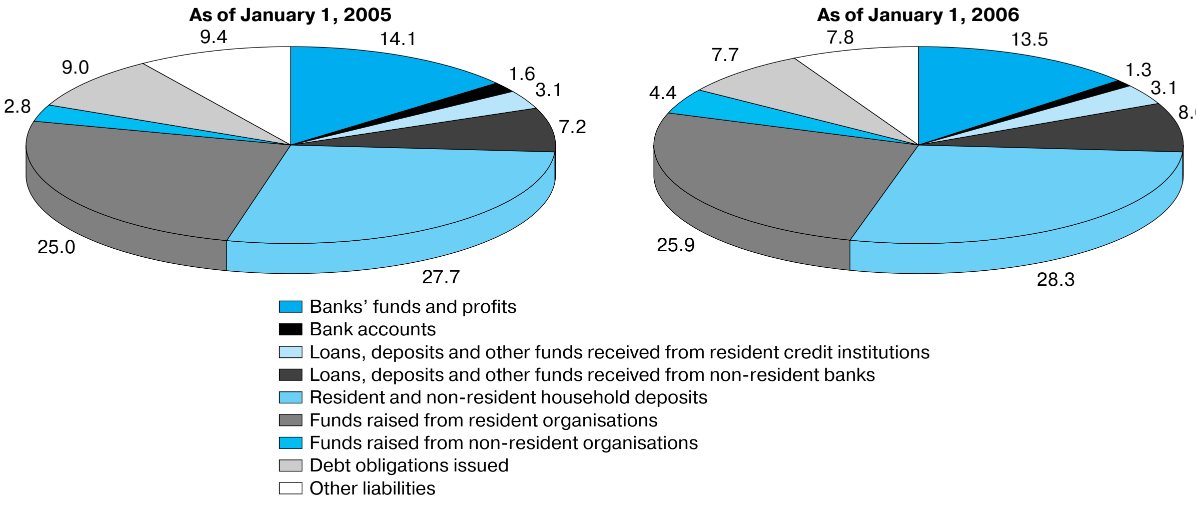
The balances in customers' accounts[14] increased 40.2% in 2005 to 5,818.9 billion rubles and their share in banking sector liabilities expanded from 58.2% to 59.7%.

Against the backdrop of the Russian economy's rapid growth funds raised from corporations[15] became the main source of the expansion of the resource base of credit institutions in 2005. These funds increased 48.7% as against 43.4% in 2004 *(see Chart 1.8).* The share of this source in banking sector liabilities expanded from 27.8% to 30.3% and these funds accounted for 37.0% of overall growth in banking sector liabilities. Funds raised from resident organisations predominated in total funds raised from the enterprise sector: over the year they increased 41.7% and as of January 1, 2006, reached 2,527.7 billion rubles.

The balances in settlement and current accounts, i.e., short-term resources, rose 31.5% and accounted for almost 57.0% of the total funds raised from organisations.

Growth in *corporate deposits* stood at 66.0% as against 80.5% in 2004 and their share in aggregate banking sector liabilities expanded from 7.9% to 9.6%. Demand deposits and deposits with a maturity of up to 30 days increased 140% to 17.5% to total deposits. Deposits with maturities from 31 days to one year grew 64.7% to 53.8% of total deposits as of January 1, 2006, and deposits with maturities longer than one year increased 42.1% to 28.7% of total deposits.

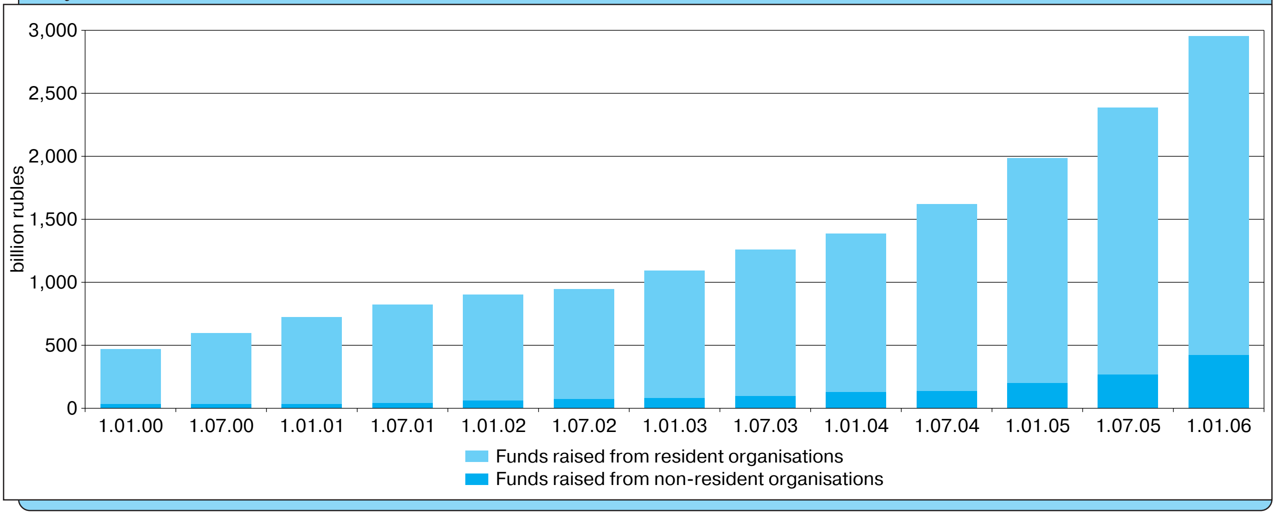
Structure of banking sector liabilities (%) *CHART 1.7*



[14] Balances in organisations' accounts, including all-level budgetary funds and extra-budgetary funds, household funds, float, factoring and forfeiting balances and funds written down from customers' accounts but not entered in a credit institution's correspondent account.
[15] Except resident credit institutions and non-resident banks.

Raising corporate funds by credit institutions

CHART 1.8



The biggest growth in corporate deposits was demonstrated by diversified banks (by 110% to 11.8% of liabilities) and state-controlled banks (by 60% to 7.3% of liabilities). The main factors of growth were a high level of customer confidence in large banks and a wider range of services provided by them. These groups of banks account for almost 62.0% of the banking sector corporate deposits.

The same factors were also behind rapid growth (by 72.7%) in corporate deposits with banks controlled by foreign capital. The share of these deposits in the foreign-controlled banks' liabilities expanded from 13.5% to 16.0%, whereas the banking sector average stood at 9.6%.

Other funds raised almost tripled in the period under review, mainly due to growth in non-resident corporate funds with maturities longer than one year, which increased from 38.5 billion rubles to 221.1 billion rubles, i.e., by 5.7 times.

Almost 80% of these funds were raised by state-controlled and diversified banks. The main source of these funds are loans on the international market by subsidiaries of large Russian banks.

At the same time, the share of other funds raised in banking sector liabilities is still small: as of January 1, 2006, it stood at 2.9% as against 1.3% as of the beginning of last year.

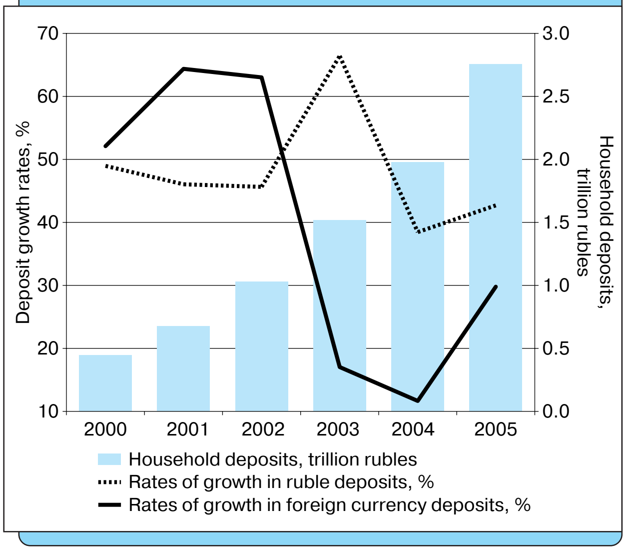
Household deposits were a major source of growth in credit institutions' resources. In 2005, they grew faster than in 2004 and increased over the year by 39.3% as against 30.3% in 2004, to 2,754.6 billion rubles. The share of this source of funds in aggregate banking sector liabilities also expanded, from 27.7% to 28.3%. At the same time, these funds accounted for almost 30% of growth in banking sector liabilities. Growth in household deposits with banks was down to factors both unrelated to the banking sector (growth in real income) and factors that were directly connected with banking. The latter included the establishment of the deposit insurance system, which was designed to boost public confidence in banks, the expansion of the bank network, greater availability and broader range of banking products and the improved quality of the services provided to households.

In the past three years, ruble-denominated household deposits have been growing considerably faster than deposits denominated in foreign currency. This trend continued in 2005 when ruble-denominated deposits increased 42.7% and deposits in foreign currency grew 29.8% (in ruble terms) *(see Chart 1.9)*. As a result, the share of ruble-denominated deposits with banks in total household deposits expanded from 73.8% to 75.6%. In 2005, household deposits with maturities longer than one year rose 45.0% and their share of total deposits from 57.2% to 59.5%.

Competition continued to increase on the household deposit market. Household deposits with banks, excluding Sberbank, expanded 58.4%, whereas household deposits with Sberbank grew 26.5%. As a result, Sberbank's share of the market, which stood at almost 60.0% at the beginning of last year, contracted to 54.4% at the end *(see Chart 1.10)*.

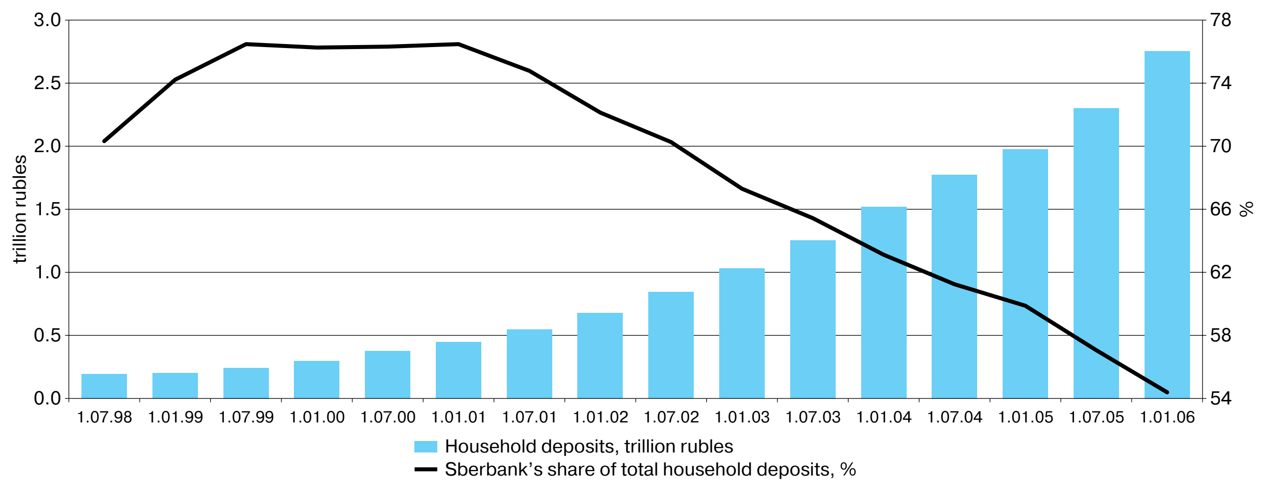
Household deposits

CHART 1.9



Household deposits with credit institutions

CHART 1.10



The highest rates of growth in household deposits were registered by the diversified banks (75.4%), intra-group banks (61.2%) and banks controlled by foreign capital (52.4%). The value of household deposits taken by medium-sized and small regional banks in 2005 increased almost 50% in 2005.

Household deposits with small and medium-sized banks based in the Moscow Region and admitted to the deposit insurance system[16] increased 47.5%. Their share in these banks' liabilities stood at 14.7% and was considerably smaller than the banking sector average.

Funds raised by credit institutions by issuing debt obligations increased 16.3% in 2005 as against 1.5% in 2004 and aggregated 749.2 billion rubles. As of January 1, 2006, the debt obligations issued by banks accounted for 7.7% of banking sector liabilities as against 9.0% as of January 1, 2005.

As before, promissory notes accounted for most of the debt obligations issued by banks (82.0% as of January 1, 2006, as against 78.6% as of January 1, 2005) and their value rose 21.4% during that period, to 614.5 billion rubles. At the same time, their share in banking sector liabilities contracted from 7.1% as of January 1, 2005, to 6.3% as of January 1, 2006.

The biggest growth (35.8%) was registered in promissory notes issued by medium-sized and small banks based in the Moscow Region. They accounted for 9.4% of these banks' liabilities, but their share in total bank notes was quite small (7.7%).

The value of bonds issued by banks increased 120% and savings certificates 80%, but their share in total banking sector liabilities remained small at 0.8% (it was 0.5% as of January 1, 2005). One reason for slow growth in the issue of bank bonds on the domestic market is the high cost of organising their issue and placing. In addition, competition has been building up from international financial markets, where credit institutions can raise funds at lower interest rates than on the domestic market.

Interbank liabilities[17] increased 47.4% in 2005 as against 40.3% in 2004 and totalled 1,086.4 billion rubles and their share in aggregate banking sector liabilities expanded from 10.3% to 11.1%.

Russian credit institutions continued actively to raise funds on the international interbank market *(see also Subsection II.3)*. The value of liabilities to non-resident banks grew 52.4% as against 36.6% in 2004 and as a result, the share of loans received from non-resident banks expanded from 69.8% to 72.2% of total interbank loans *(see Chart 1.11)*. This source of funds accounted for 8.0% of banking sector liabilities as of January 1, 2006, as against 7.2% as of January 1, 2005. More than two-thirds of the value of loans on the international interbank market were received for a term of one year and more (68.9% as of January 1, 2006, as against 57.5% as of January 1, 2005).

As state-controlled and diversified banks had high international credit ratings, the value of loans they received increased 100.0% and 45.8% respectively and these banks accounted for 65.4% of total loans received on the international interbank market.

The balances of funds raised on the domestic interbank market increased 35.7% in 2005, but their share in banking sector liabilities remained virtually unchanged at 3.1%.

I.3.2. Asset dynamics and structure

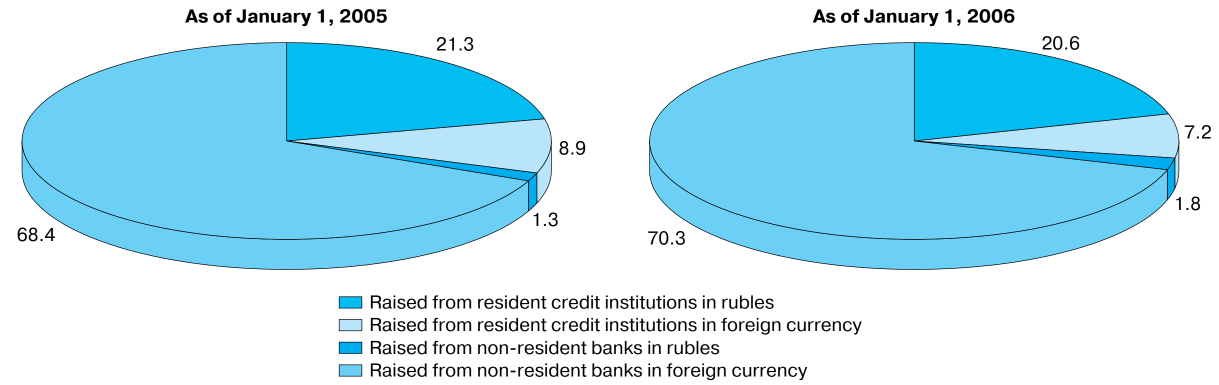
The Russian banking sector managed on the whole to maintain positive development dynamics and strengthen its positions in the system of financial intermediation in 2005.

The structure of banking sector assets is shown in *Chart 1.12.*

[16] Of total small and medium-sized banks based in the Moscow Region, 59% have been admitted to the deposit insurance system, 29% have not and 12% had no licence to conduct operations with household funds.
[17] Obligations on loans, deposits and other funds raised on the interbank market.

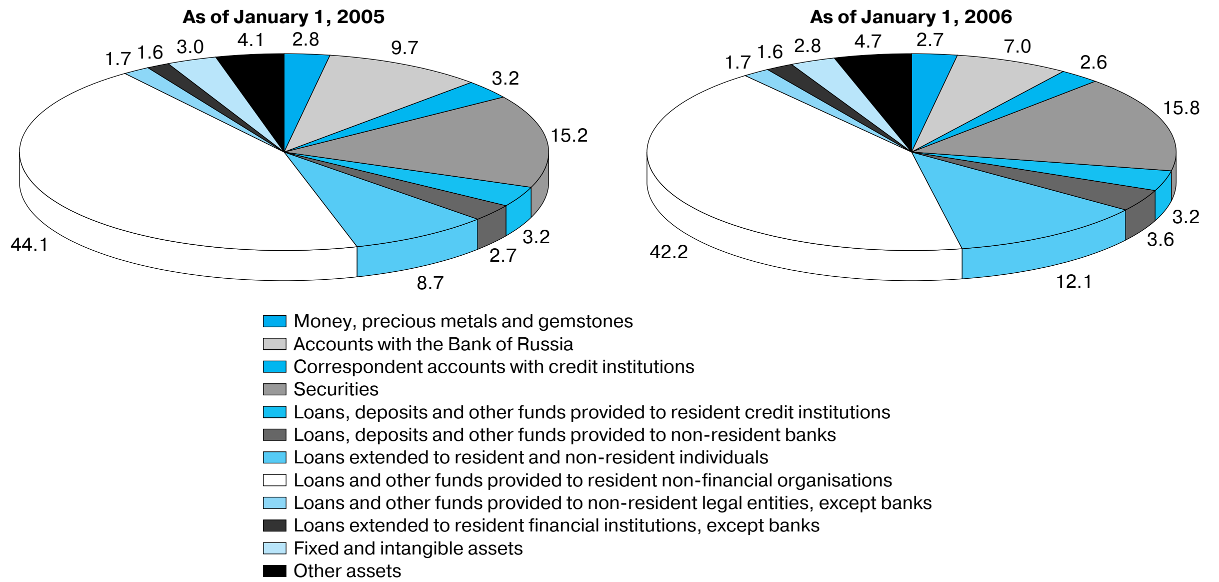
Loans, deposits and other funds raised on interbank markets (% share in total value)

CHART 1.11



Banking sector asset structure (%)

CHART 1.12



Diversified banks and banks controlled by foreign capital registered the highest rate of growth in assets (53.6% and 46.4% respectively), far surpassing the banking sector average. State-controlled banks increased assets by 36.8%. The assets of medium-sized and small regional banks expanded at rates that were slightly slower than the banking sector average.

The primary orientation of intra-group banks to the provision of services to affiliated structures is a factor containing the development of this group of banks, whose assets increased 28.9% in 2005.

The expansion of lending was the main factor of growth in banking sector assets in 2005. Sectoral distribution of loans is shown in *Chart 1.13.*

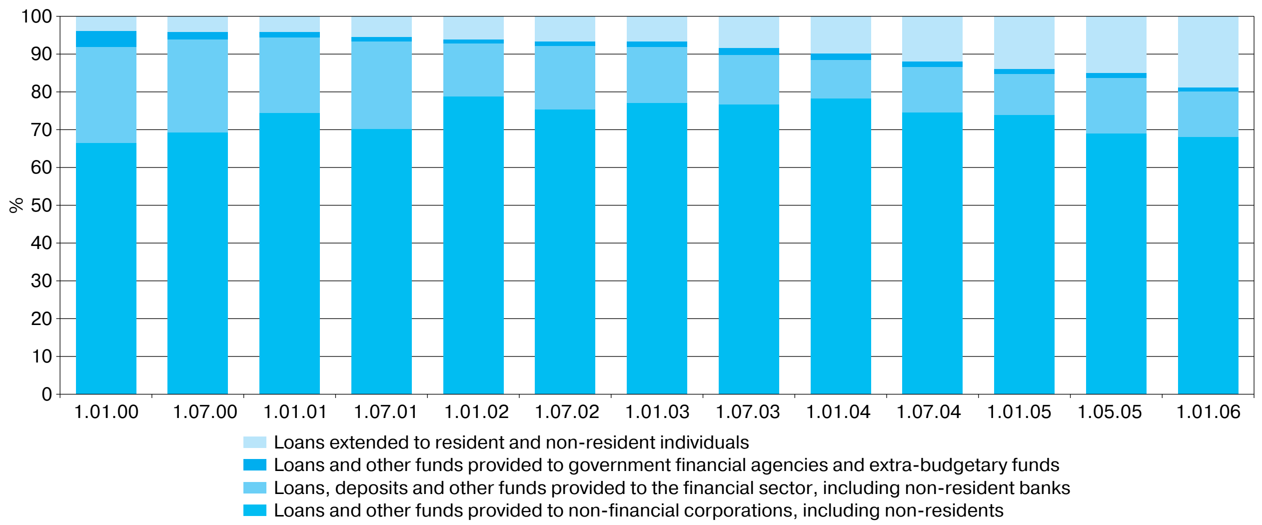
Loans extended by Russian banks to non-financial corporations increased 30.5% in 2005 as against 39.0% in 2004 and totalled 4,110.6 billion rubles as of January 1, 2006, whereas its share in aggregate banking sector assets contracted from 44.1% to 42.2% over the year. Almost 69% of operating credit institutions expanded loans to non-financial corporations. Although foreign currency loans grew faster than ruble-denominated loans (38.7% as against 27.4%), 70.7% of total corporate loans were extended in the national currency.

Loans with maturities longer than one year accounted for 43.5% of total corporate loans (as against 39.5% as of the beginning of 2005) and their rates of growth (43.7%) exceeded by far overall growth in loans. This process points to the economy's unabated demand for investment.

State-controlled and diversified banks are the principal creditors of the non-financial sector of the economy, accounting for 46.7% and 22.4% of total corporate loans respectively. Loans extended to the non-financial sector by these banks account for 48.4% and 37.6% of their assets respectively. The highest rates of growth in corporate loans, exceeding the banking sector average, were demonstrated by banks controlled by foreign capital (55.1%), state-controlled banks (33.9%) and regional small and medium-sized banks (38.9%).

Sectoral distribution of loans (as % of total credit)

CHART 1.13



The manufacturing sector accounted for 20.2% of total credit institutions' outstanding loans as of January 1, 2006, the construction sector 5.7%, the mining sector 4.3%, and agriculture, hunting and forestry 3.7%. Wholesale and retail trade establishments and car, motorcycle, household appliances and personal goods repair firms accounted for the largest part of total debt (29.8%).

It should be emphasised that the slowdown of lending to the non-financial sector in 2005 was the result of banks' increased consumer lending and investment in corporate securities amid intense competition from international creditors of Russian non-financial corporations. The assigning to Russia of the investment grade rating by leading world rating agencies in 2005 gave a fresh impetus to eurobond placements, which became a major source for financing the long-term borrowings of Russia's big business. First of all this applies to industrial corporations, which have a high credit rating on the world financial market.

Loans and other funds placed with non-resident legal entities in 2005 increased 38.1% to 164.1 billion rubles, of which 88.8% of placements were in foreign currency. The share of loans to non-resident legal entities in banking sector assets was small (1.7% as of January 1, 2006).

Lending to households continued to expand rapidly in 2005. Loans to resident individuals[18] increased 90.0%, from 616.5 billion rubles as of January 1, 2005, to 1,174.9 billion rubles as of January 1, 2006. Loans to households are largely extended in rubles (85.2% of their total volume). The share of loans to households in aggregate banking sector assets expanded from 8.6% as of January 1, 2005, to 12.1% as of January 1, 2006, and in total banking sector loans from 13.8% to 18.4%.

Most of banking sector loans to resident individuals were extended by state-controlled banks (48.8%), diversified banks (24.5%), intra-group banks (9.4%) and banks controlled by foreign capital (8.4%). At the same time, lending to households was expanded at the most rapid rates in 2005 by diversified banks, which increased loans 180% in volume, banks controlled by foreign capital, which almost doubled loans, and state-controlled banks, which registered an 80% increase in loan volume. Large banks have a competitive edge on the retail services market due to their extensive branch network, diversified resource base and highly-qualified management, and advanced banking technologies including in the risk control field.

Total loans extended to the non-financial and household sector increased 40.3% to 5,454.0 billion rubles in 2005. Its share in aggregate banking sector assets expanded from 54.5% to 55.9% and relative to GDP from 22.9% to 25.3%.

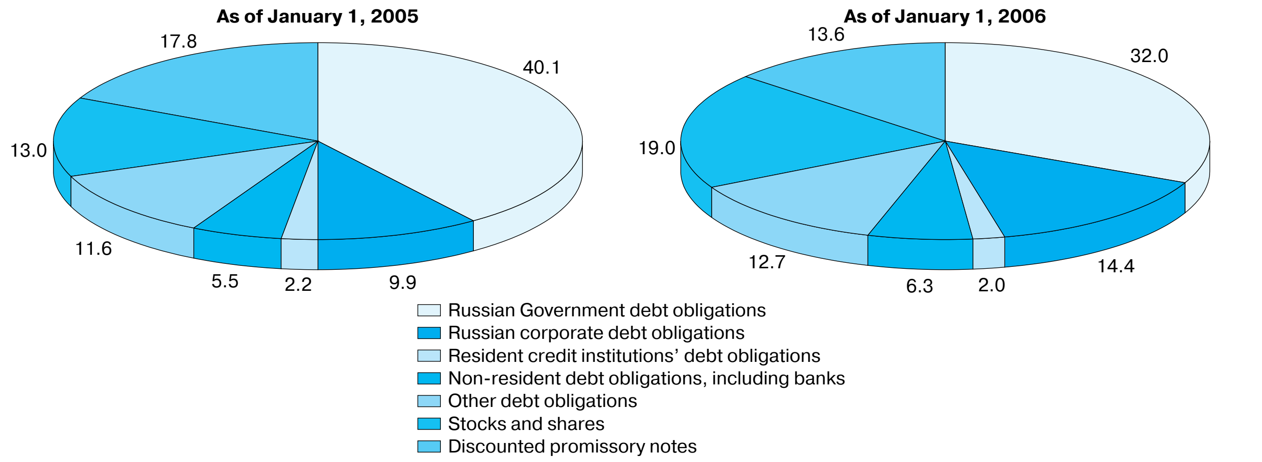
Credit institutions continued to be proactive on the securities market in 2005. Their investments in securities increased 41.6% over the year (as against 8.4% in 2004) to stand at 1,539.4 billion rubles as of January 1, 2006, and their share in banking sector assets expanded slightly (from 15.2% to 15.8%).

The share of investments in debt obligations contracted in 2005 from 69.2% to 67.3% of credit institutions' securities portfolios and the share of discounted promissory notes shrank from 17.8% to 13.6%; the share of investments in stocks and shares expanded from 13.0% to 19.0% *(see Chart 1.14).*

The structure of credit institutions' investments in debt obligations changed significantly. While the value of bank investments in federal government debt instruments increased 13.0% to 492.0 billion rubles, their share contracted from 6.1% to 5.0% of aggregate banking sector assets and from 57.9% to 47.5% of total bank investments

[18] Including loans to private entrepreneurs.

Structure of investments in securities (including discounted promissory notes), % CHART 1.14



in debt obligations. Investments in corporate bonds ensured almost 40% of growth in bank investments in debt obligations. Against the backdrop of upward price dynamics, investments in corporate bonds increased almost 110% as against 80% in 2004, to 221.5 billion rubles, and their share in aggregate banking sector assets expanded from 1.5% to 2.3%.

As the RTS index rose, investments in stocks and shares[19] increased 110% as against 21.7% in 2004, to 292.8 billion rubles, but their share in banking sector assets remained small (3.0% as of January 1, 2006, as against 2.0% as of January 1, 2005). Investments in the shares of Russian non-financial corporations accounted for 41.3% of total investment, 12.2% in the shares of resident credit institutions and 9.0% in the shares of non-resident banks. Placements for investment purposes (controlling shareholding) were largely made in the shares of resident credit institutions and non-resident banks, whereas investments for subsequent resale were made in the shares of Russian non-financial corporations, especially blue chips.

Growth in banks' investments in discounted promissory notes (8.6%) was considerably smaller than in other active operations in 2005. The share of discounted notes in banking sector assets contracted from 2.7% to 2.2% over the year. Discounted notes of Russian banks accounted for 67.9% of the discounted note portfolio (as against 49.2% in 2004) and their value increased 50% to 142.6 billion rubles. At the same time, investments in discounted notes of other Russian enterprises decreased almost 29.0% and their share in total discounted notes contracted from 46.8% to 30.6% over the year. Credit institutions reduce investments in discounted notes of non-financial corporations to improve the quality of their credit portfolios[20].

Having reduced their investments in Russian non-financial corporation notes by more than a half (55%), the state-controlled banks increased investments in Russian banks' notes by 14.7%. Intra-group banks increased investments in Russian banks' notes by 81.0%, diversified banks by 49.3% and medium-sized and small banks based in the Moscow Region by 58.0%.

Claims on interbank loans rose 56.9% in the banking sector as a whole in 2005 (as against 61.5% in 2004) and amounted to 668.0 billion rubles and their share in banking sector assets expanded from 6.0% to 6.9%. This growth was largely due to a 79.5% increase in the funds placed with non-resident banks, whose share in banking sector assets expanded from 2.7% to 3.6%. It should be noted that mostly short-term funds are placed with non-resident banks: only 14% of total loans to non-resident banks were placed for a maturity longer than one year as of January 1, 2006.

Diversified banks were particularly proactive on international financial markets: the value of funds they placed with non-resident banks in 2005 increased 120%. This group of banks placed 37.7% of total loans extended to non-resident banks. Banks controlled by foreign capital increased their placements with non-resident banks by 94.0% and state-controlled banks by 66.3%.

The value of loans placed on the domestic interbank market grew 37.6% and their share in banking sector assets was virtually unchanged at 3.2%.

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[19] Here and below, investments in stocks and shares include majority shareholding.
[20] Under Bank of Russia Regulation of March 26, 2004, No. 254-P "On the Procedure for Making by Credit Institutions Loan Loss Provisions, Provisions for Loan Debts and Similar Debts", the promissory notes of legal entities (except credit institutions) are classified in Loan Quality Category III (doubtful) and lower.

I.4. Financial Performance of Credit Institutions

I.4.1. Financial results

In 2005, growth in banking sector profits was the biggest over the past three years (47.3% as against 38.6% in 2004).

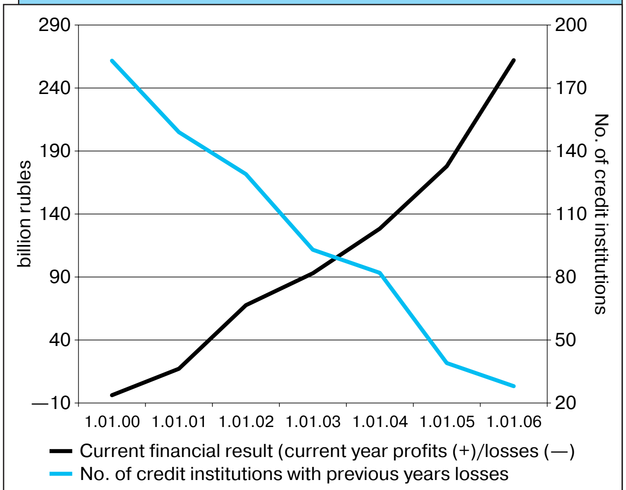
Rapid rates of profit growth were typical of all groups of banks, but intra-group banks' profits increased 2.1 times faster the banking sector average and diversified banks' profits grew 1.6 times faster.

The profits of operating credit institutions stood at 262.1 billion rubles in 2005 *(see Chart 1.15)* and taking into account the financial result of the previous years, it amounted to 304.5 billion rubles (as against 177.9 billion rubles and 199.4 billion rubles in 2004 respectively).

The share of profit-making credit institutions expanded from 98.2% to 98.9% of total credit institutions in 2005, whereas the number of loss-making credit institutions fell from 22 to 14 and their share contracted from 1.7% to 1.1% of total credit institutions. However, the total losses of operating credit institutions increased from 600 million rubles in 2004 to 7.9 billion rubles in 2005. Most of the losses (about 95.0%) were incurred by a large bank in the process of reorganisation and expansion.

The distribution of the various groups of banks from the standpoint of the financial result corresponds on the whole to their position in the banking sector in terms of assets. The biggest contribution to the financial result (39.4%) was made by the state-controlled banks, which accounted for 40.7% of banking sector assets; diversified banks contributed 27.1% and their share in banking sector assets stood at 25.1%; intra-group banks contributed 18.5% (their share in banking sector assets was 16.2%).

Banking sector financial result *CHART 1.15*



Banking sector efficiency indicators continued to improve due to high rates of growth in profits. The return on credit institutions' assets increased from 2.9% in 2004 to 3.2% in 2005 and the return on equity grew from 20.3% to 24.2%[21], which shows that the banking sector is becoming increasingly attractive to investors. In the year under review, 562 banks, or 44.9% of the total, increased their return on assets and 671 banks, or 53.6% of the total, increased their return on equity.

Intra-group and diversified banks improved their profitability indicators significantly. The return on assets in these two groups of banks in 2005 reached 3.6% and 3.7% respectively, the highest levels in the banking sector (2.3% and 3.6% in 2004 respectively). The return on equity increased from 13.1% to 22.2% in intra-group banks and from 22.3% to 30.8% in diversified banks in 2005.

Banks controlled by foreign capital ceased to be the most profitable banks in 2005. Compared to 2004, the return on assets in this group of banks decreased from 3.7% to 2.9% and the return on equity from 28.7% to 20.8%, because growth in their financial result (10.0% over 2005) was 4.7 times smaller than the banking sector average. This was due, to some extent, to significant growth in their expenditures on the development of retail and other service infrastructures.

The profitability indicators of state-controlled banks were close to the banking sector average: their return on assets was 3.1% and on equity 28.4%.

Medium-sized and small regional banks remain far more profitable than medium-sized and small banks based in the Moscow Region. The return on equity of the medium-sized and small regional banks was 16.7% in 2005 and the return on assets 3.0% (15.8% and 3.0% in 2004 respectively). The return on assets of the Moscow-based medium-sized and small banks fell slightly (from 2.3% in 2004 to 2.1% in 2005) and the return on equity was down from 9.0% to 8.7%. The Moscow-based medium-sized and small banks are the least profitable banks in Russia.

I.4.2. Income and expense structure

Income from foreign exchange dealing continued to account for the largest part of credit institutions' *gross*

[21] Return on assets is calculated as the ratio of the full-year pre-tax financial result to bank assets and the return on equity is calculated as the ratio of the full-year pre-tax financial result to regulatory capital. Assets and capital have been calculated as annual (chronological) averages for the reporting period.

income (45.1% in 2005 as against 37.3% in 2004). This was the result of the favourable situation on the domestic foreign exchange market, brought about by a massive inflow of exporters' foreign currency earnings, and the world currency market, which led to growth in credit institutions' operations with foreign exchange and foreign currency values and a corresponding increase in income from these operations. However, the share of net income (income less expense) from foreign exchange operations in banking sector net current income was small (see more below).

The recovery of sums from fund and reserve accounts continued to account for a large part of gross income in 2005 (27.0% as against 34.0% in 2004).

Expenses on foreign exchange operations, whose share expanded from 38.7% to 46.9%, and expenses on deductions to funds and reserves, whose share contracted from 37.7% to 30.8%, accounted for the largest part of expenses in 2005. There was a significant contraction in the share of expenses on securities trading (from 5.4% to 3.9%). Expenses on interest payments on borrowings (their share stood at 5.6% in 2005 as against 5.9% in 2004) and administrative expenses, whose share contracted from 4.5% in 2004 to 4.2%, decreased slightly over the year in relative terms.

Net current income of credit institutions[22] is a more revealing indicator for analysis. In 2005 it increased 42.4% year on year, to 665 billion rubles. Its structure was largely determined by the further expansion of lending, growth in banks' investments in securities and increase in banking commissions *(see Chart 1.16)*.

Net interest income is the main element of net current income of credit institutions and its share in net income expanded slightly in 2005 (from 62.3% in 2004 to 63.0%). The slowing of growth in interest expenses on household deposits, caused by a drop in interest rates[23], seriously affected growth in net interest income.

State-controlled banks significantly expanded the share of net interest income (from 66.4% to 73.7%). In banks controlled by foreign capital the share of this income increased from 51.0% to 53.5%. Other groups of banks reduced slightly the share of interest income in total net income.

Net commission income and its share in net income of credit institutions continued to increase (one reason for this is the expansion of retail services). Net commission income is second to interest income, exceeding net income from investments in securities and operations with foreign exchange. The share of net commission income in net income expanded from 22.6% as of January 1, 2005, to 23.2% as of January 1, 2006.

All groups of banks, except intra-group banks, registered growth in net commission income. This kind of income is particularly important for banks controlled by foreign capital due to the significant expansion of retail services provided by this group of banks. As a result, their share increased from 22.6% to 26.0%.

As a result of growth in operations with foreign exchange and securities, net income from these operations increased, but its share in net current income remained virtually unchanged.

It appears that a decline in net income from the purchase and sale and revaluation of securities came to an end in 2005. The share of this income in total net current income contracted from 12.5% in 2004 to 12.4%. This was largely due to the restructuring of investments in securities: the share of investments in government securities contracted, whereas the share of investments in higher-yield shares and corporate bonds expanded.

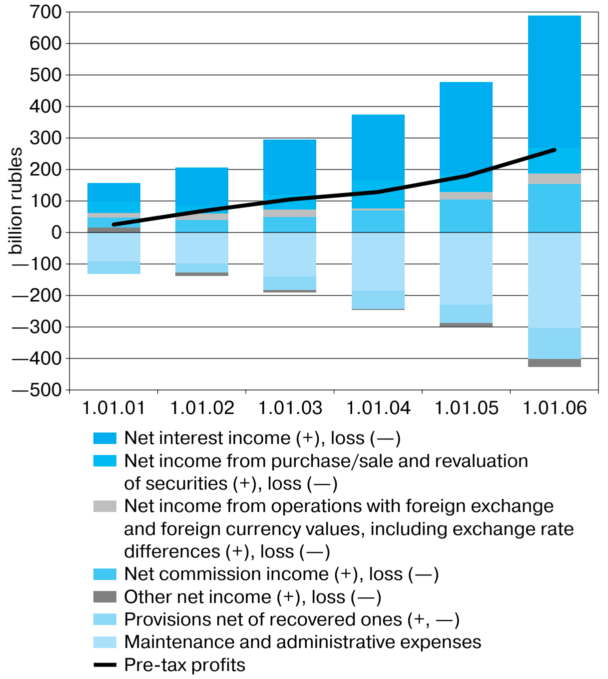
Intra-group banks and diversified banks posted the biggest growth in the share of this income in total net current income in 2005 (from 14.0% to 17.3% and from 17.2% to 23.0% respectively). State-controlled banks continued to reduce the share of income from securities trading in net current income (in 2005, it stood at 7.2% as against 13.0% in 2004).

The share of credit institutions' net income from operations with foreign exchange and foreign currency values, including the exchange rate differences, remained stable at 5.1% in 2005 (it was 4.9% in 2004).

This income is most important for the banks controlled by foreign capital, although the share of income derived by these banks from foreign exchange

Structure of current financial result (net income and profits) of credit institutions

CHART 1.16



[22] Net income is the financial result before making (recovering) provisions net of maintenance and administrative expenses. Calculated in accordance with the Profit and Loss Statement of Credit Institutions (form code 0409102).

[23] An average weighted interest rate on ruble-denominated household deposits with all maturities, except demand deposits, decreased from 9.2% p.a. in January 2005 to 7.4% p.a. in December 2005.

dealing contracted from 21.5% to 19.1% in 2005. At the same time, the role played by income from foreign exchange dealing in net current income changed dramatically in the medium-sized and small banks of the Moscow Region: its share in net income of this group of banks expanded from 6.4% in 2004 to 19.1%[24]. The intra-group banks' income from foreign exchange operations accounted for 2.1% of the groups' net current income, whereas in 2004 intra-group banks registered a 1.3% loss of net current income on these operations.

The maintenance and administrative expenses of credit institutions increased 31.9% in 2005 as against 24.1% in 2004, but relative to net current income they declined from 49.2% in 2004 to 45.5%.

Maintenance and administrative expenses were cut by all groups of banks in 2005, except intra-group banks and banks controlled by foreign capital, in which these expenses remained virtually unchanged. Medium-sized and small regional banks have the highest maintenance and administrative expenses (62.4% of net current income).

In 2005, the value of provisions made by credit institutions (net of recovered ones) increased 72.2% to 100.0 billion rubles and the ratio of provisions to net income expanded from 12.4% to 15.0%. Last year's growth in provisions indicates, to some extent, that credit risk had increased and that banks had taken a more conservative approach to the evaluation of the quality of their loan portfolios to qualify for admission to the deposit insurance system[25].

This is particularly obvious in the group of banks controlled by foreign capital and state-controlled banks, which registered slower growth in profits due to the significant increase in provisions previously maintained at a low level. The ratio of provisions to net income in the banks controlled by foreign capital stood at 15.4% in 2005, whereas in 2004 the recovered provisions of these banks exceeded the provisions they made. The ratio of provisions to net income in the state-controlled banks grew from 6.7% to 15.2%.

The grouping of credit institutions by financial soundness changed in 2005 owing to the measures taken to assess the financial soundness of credit institutions for admission to the deposit insurance system. The number of credit institutions without any shortcomings (Group 1) decreased from 352 to 218, whereas the number of credit institutions with few shortcomings (Group 2) rose from 904 to 986. Overall, financially sound credit institutions (Group 1 and Group 2) accounted for 96.1% of the total number of operating banks in 2005 as against 96.7% a year earlier. The share of problem banks (Group 3 and Group 4) expanded slightly over the year (from 3.2% in 2004 to 3.9%).

Overall, the share of financially sound credit institutions in aggregate banking sector assets remained large (99.6%) in 2005.

[24] As Moscow-based medium-sized and small banks stagnate as far as lending, securities trading and settlements are concerned, the role of foreign exchange dealing inevitably increases. This applies, in particular, to the currency exchange operations (a list of the banks that are the principal players on the Moscow spot currency market bears this out).

[25] The share of loan loss provisions expanded significantly in total provisions (net of recovered ones) in 2005 (from 93.2% to 98%). In 2004, growth in lending activity was not accompanied by corresponding growth in provisions, which remained unchanged on the previous year.

II

Banking Sector Risks

II.1. Credit Risk

II.1.1. Overdue loan debts

The credit risk of Russia's banks remains moderate. While loans and other placements increased 42.7%, overdue loan debt expanded 23.4% in 2005 and as of January 1, 2006, it stood at 76.4 billion rubles. At the same time, its share in total loan debt contracted from 1.4% to 1.2%.

Banks that have prime borrowers have more chance of getting their credit back. Intra-group banks saw the share of overdue debt contract in their credit portfolios in 2005 from 1.5% to 1.3% and this share narrowed even more in state-controlled banks (from 1.7% to 1.1%). The share of overdue debt in other groups of banks expanded in the year. Medium-sized and small banks based in the Moscow Region and other regions had the largest share of overdue debt (1.6% as of January 1, 2006, as against 1.3% as of January 1, 2005, and 1.7% as of January 1, 2006, as against 1.5% as of January 1, 2005 respectively). The most rapid growth in the share of overdue debt was registered in the banks controlled by foreign capital (from 0.7% as of January 1, 2005, to 1.1% as of January 1, 2006), largely because total loan debt increased significantly in this group. In addition, most of the banks controlled by foreign capital have higher accounting standards.

The number of credit institutions with overdue debt accounting for less than 4%[26] of their credit portfolio declined slightly (from 753 as of January 1, 2005, to 741 as of January 1, 2006) and the share of these banks in banking sector assets remained virtually unchanged at 91.2% as against 91.6% as of January 1, 2005.

There was also a slight fall (from 56 to 54) in the number of credit institutions with an overdue debt of more than 8% in their credit portfolios. These banks accounted for 1.2% of banking sector assets as of January 1, 2006. At the same time, in most of them real loan loss provisions and the value of collateral almost equalled overdue debt.

The level of credit risk of Russia's banks is still primarily affected by the quality of loans extended to the sector of non-financial corporations, which accounted for 43.8% of aggregated banking sector assets as of January 1, 2006, or more than two-thirds of the total value of the loans extended. Overdue debt accounted for 1.3% of loans to the sector of non-financial corporations as of January 1, 2006, as against 1.5% at the beginning of last year. As regards ruble-denominated loans, this indicator remained virtually unchanged (1.5% as of January 1, 2006, and 1.6% as of January 1, 2005), whereas the share of overdue debt in foreign currency-denominated loans contracted from 1.4% to 0.8%. In terms of the borrowers' activity category *(see Chart 2.1),* the largest share of overdue debt was registered in 2005, as in the previous years, on ruble loans to agriculture[27] (2.2% in 2005 as against 2.9% in 2004), construction (1.8% in 2005 as against 1.5% in 2004) and trade and public catering[28] (1.7% in 2005 as against 2.3% in 2004). The share of overdue debt on loans extended in foreign currency to agriculture[29] expanded significantly in 2005 (from 0.5% as of January 1, 2005, to 2.3% as of January 1, 2006). At the same time, the share of overdue debt in foreign currency loans to the construction sector contracted from 6.5% as of January 1, 2005, to 1.1% as of January 1, 2006.

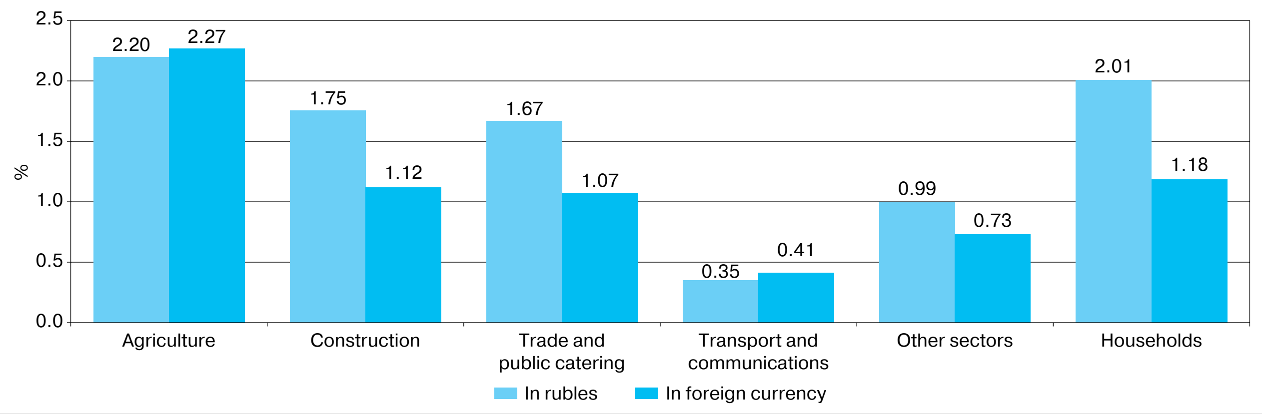
Overdue debt on loans to households increased rapidly in 2005 and its share in total loans expanded from 1.4% as of January 1, 2005, to 1.9% as of January 1, 2006. The share of overdue debt on ruble credit to households expanded from 1.3% as of January 1, 2005, to 2.0% as of January 1, 2006, and on foreign currency loans contracted from 1.6% to 1.3%.

The risk monitoring of lending to the sector of non-financial corporations by the 200 largest banks in terms of assets revealed 41 banks with a potentially high level of credit risk[30] as of January 1, 2006. These banks accounted for 17.7% of aggregate banking sector assets. An analysis of the credit risk concentrations showed that in 29 of these 41 banks the share of loans to financially unsound borrowers in total classified loans exceeded the average for the 200 largest banks.

The risk monitoring of lending to individuals also put in the risk group[31] 41 banks of the 200 largest banks by assets[32]. These banks accounted for 16.1%

[26] Threshold values 4% and 8% were established by monitoring the bank exposure in lending to non-financial enterprises.
[27] From January 1, 2005, agriculture, hunting and forestry.
[28] From January 1, 2005, wholesale and retail trade and car, motorcycle, household appliances and personal goods repairs.
[29] From January 1, 2005, agriculture, hunting and forestry.
[30] Banks whose failure to recover overdue debt may lead to the reduction of capital adequacy to dangerously low levels (less than 12%).
[31] As in the case of risk monitoring of lending to the sector of non-financial corporations, the risk group comprises banks in whose failure to recover overdue debt may lead to the reduction of capital adequacy to levels lower than 12%.
[32] These are not the same banks as indicated above.

Overdue debt in debt on loans by borrowers' activity category as of January 1, 2006 (%) CHART 2.1



of aggregate banking sector assets. In 10 out of these 41 banks the share of loans to households exceeded 10% and the ratio of overdue debt to own funds (capital) was more than 5%. These 10 banks accounted for 2.35% of aggregate banking sector assets.

II.1.2. Credit portfolio quality

As of January 1, 2006, standard loans accounted for 48.2% of banking sector loan debt and non-performing loans (problem and bad loans) 3.2% (46.9% and 3.8% as of January 1, 2005 respectively). This level is considerably lower than the credit risk level that may provoke a bad debt crisis[33] *(see Chart 2.2).* When evaluating the situation, allowances should be made for the quality of credit institutions reporting. Nevertheless, even in that case the risk of a bad debt crisis is now low.

As of January 1, 2006, the largest share of non-performing loans was in the credit portfolios of intragroup banks (4.4% of total loans). In the banks controlled by foreign capital, non-performing loans accounted for 0.8% of their credit portfolio and these banks also had the largest share of standard loans (62.5%).

There were 480 credit institutions with standard loans comprising more than half of their credit portfolios. These banks accounted for 33.6% of aggregate banking sector assets. In comparison, there were 460 such credit institutions in 2004 and they accounted for 55.8% of aggregate banking sector assets.

The number of credit institutions with a share of standard loans exceeding 50% increased mostly due to the Moscow-based and regional medium-sized and small banks. This was, to some extent, the result of tightened requirements for the quality of credit institutions' credit portfolios in connection with their admission to the deposit insurance system.

II.1.3. Credit risk concentration

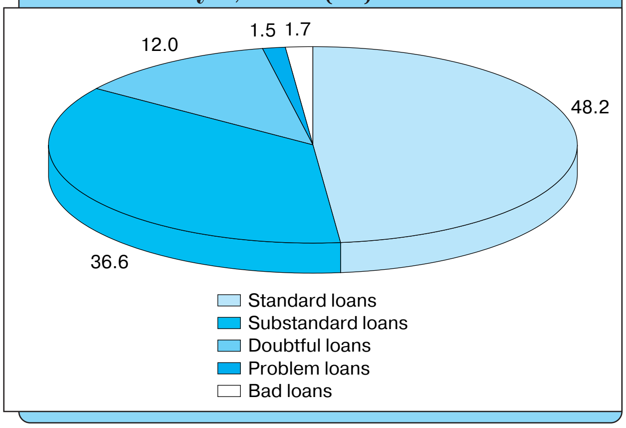
None of the credit institutions violated the maximum major credit risk ratio[34] (N7) in 2005 (there was one as of the beginning of last year).

Over the year, major credit exposures (credit risks) of the banking sector increased by 29.6% from 2,298.2 billion rubles to 2,978.1 billion rubles and overall loan debt grew 42.7%. As a result, major credit in aggregate banking sector assets contracted from 32.2% as of January 1, 2005, to 30.5% as of January 1, 2006.

Large credit exposures accounted for the largest part of bank assets in the medium-sized and small banks of the Moscow Region (45.6%) and the smallest in the state-controlled banks (20.8%).

According to reported data, the number of credit institutions that violated the N6 ratio (maximum risk per borrower or group of connected borrowers) declined from 23 to 13 and their share in aggregate banking sector as-

Quality of banking sector credit portfolio as of January 1, 2006 (%) CHART 2.2



[33] In international banking supervision practice non-performing loans exceeding 10% of the total loan portfolio denote a high credit risk.
[34] Under Article 65 of the Federal Law "On the Central Bank of the Russian Federation (Bank of Russia)", a major credit risk is the sum of loans, guarantees and sureties provided to one client in excess of 5% of a bank's regulatory capital.

sets contracted from 5.9% at the beginning of last year to 5.3%.

II.1.4. Shareholder- and insider-related credit risks

As of January 1, 2006, the N9.1 ratio (maximum loans, bank guarantees and sureties provided by a credit institution or banking group to its members or shareholders) was calculated by 479 credit institutions (500 credit institutions as of January 1, 2005). None of the credit institutions as of the beginning or the end of 2005 was found guilty of failing to comply with this ratio (its threshold level is set at 50%).

The N10.1 ratio, which sets a limit on total loans extended by a credit institution to insiders and guarantees and sureties issued to them, was calculated by 936 credit institutions as of January 1, 2006 (932 credit institutions as of January 1, 2005). As of the end of 2005, none of the banks failed to comply with this ratio, whereas at the beginning of last year two credit institutions were found guilty of violating it.

II.1.5. Loan loss provision

Loan loss provision levels remained high throughout 2005. The loan loss provisioning levels of most of the credit institutions virtually on all reporting dates matched the minimum required level[35]. As of January 1, 2006, the number of banks that had made a loan loss provision of at least 100% of the estimated provision adjusted to the collateral factor stood at 1,186 and they accounted for 98.4% of banking sector assets (1,203 banks and 95.4% of banking sector assets as of January 1, 2005).

Total loan loss provisions accounted for 5% of actual loan debt and 64% of non-performing (problem and bad) loans as of January 1, 2006 (68% as of January 1, 2005)[36].

According to expert judgement, some credit institutions continued to understate their balance sheet profits (possibly to have their profit tax reduced) by increasing provisions for possible losses on loans and similar debts as of the quarterly dates. In 2005, the number of credit institutions suspected of using this tax evasion scheme increased from 22 to 26 and the average understated profits increased from 368 million rubles to 447.0 million rubles. Only three of these banks are among the 200 largest in terms of assets.

II.1.6. Risks connected with corporate finance

The financial position of the corporate borrowers monitored by the Bank of Russia were generally better than in 2004. The overall conclusion is that their financial position improved last year. Industrial and communications enterprises had the best position at the end of last year, whereas enterprises in other sectors, notwithstanding improved finances, faced serious problems.

The total assets of enterprises increased in 2005 and the capital assets were covered by investment resources[37]. Only construction and communications enterprises did not have enough investment resources at the end of 2005.

The actual level of ***self-financing*** of enterprises[38], which is reflected by the net worth to assets ratio, was reasonably high, but it fell slightly in 2005 and at the end of the period stood at 69%. Only industrial and agricultural enterprises had sufficient net worth to the capital assets ratio.

The debt to net worth ratio of enterprises increased slightly in 2005 but remained moderate at 0.5 rubles. Only construction enterprises and trade and catering establishments registered a significant increase in the debt burden. At the end of the year, a moderate debt burden was typical mostly of industrial enterprises, but other enterprises carried a heavy debt burden. Transport and communications enterprises had a debt burden of 0.9 rubles. As of the end of 2005, liabilities exceeded the net worth of construction enterprises by 60% and trade and catering establishments by 200%.

The raising of mostly long-term funds, including bank credit, allowed enterprises to finance not only current operations, but also investment assets. The working capital increased by 25% in 2005 and as a result, the floating capital increased from 45.2% to 50.2%. Only construction, transport and communications enterprises had no working capital.

Enterprises' settlements improved to some extent in 2005 due to a significant reduction in overdue accounts receivable. Only trade and catering establishments registered an increase in overdue accounts receivable. Despite growth in short-term accounts receivable, overdue receivables to total receivables ratio decreased from 16% to 13%.

The short-term net-debtor position[39] in settlements increased in the period under review, a process typical of industrial enterprises, above all.

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[35] Beginning from reporting as of September 1, 2004, the minimum loan loss provision has been determined by adjusting the estimated provision taking into account the collateral factor in compliance with Bank of Russia Regulation No. 254-P, dated March 26, 2004, "On the Procedure for Making by Credit Institutions Loan Loss Provisions, Provisions for Loan Debts and Similar Debts".
[36] Allowing for the collateral factor and imputed problem loan provision, which accounts for 51% to 100% of the principal amount of debt, depending on the extent of loan depreciation.
[37] The sum of net worth and long-term liabilities.
[38] The share of net assets in the enterprise balance sheet total.
[39] The excess of accounts receivable over accounts payable.

Indicators of corporate borrowers' finances (%)

TABLE 2.1

Indicator	2005	
	Beginning of year	End of year
Self-financing ratio*	71	69
Debt to net worth**	0.41	0.45
Liabilities to banks in enterprises' total liabilities	35.9	38.4
Cash to current liabilities	8	6
Current liquidity ratio	194	211
Return on assets***	10	
Return on equity capital***	15	

** Net worth to assets.*
*** Liabilities to net worth.*
**** Over year.*

Enterprises' earnings from the sale of goods, works and services increased 21% in 2005 year on year as against 25% in 2004. The slowing of growth in earnings amid growth in expenses led to the net outflow of funds in 2005.

Net cash outflow of enterprises accounted for 0.1% of earnings and led to the reduction of cash assets by almost 3%. Net cash outflow was registered mainly in industry, whereas in other sectors net cash inflow led to an increase in enterprises' cash assets.

The current assets to current (short-term) liabilities ratio (net of overdue accounts receivable) improved and rose to 211% in 2005, whereas at the end of 2004 it stood at 204%. Only construction, transport and communications enterprises did not have enough current assets (net of overdue receivables) to cover their current (short-term) liabilities. The communications enterprises had the lowest ratio (74%).

The cash assets to current (short-term) liabilities ratio (or current liquidity ratio) decreased from 8% to 6% in 2005 as a result of net cash outflow.

Profits were the **financial result** of enterprises' activity before tax and in 2005 it increased 24% year on year (in 2004, profits rose 50% year on year). Only agricultural enterprises registered a fall in profits.

Enterprises' return on assets[40] stood at 10% in 2005 as against 12% in 2004 and the return on equity capital fell from 17% in 2004 to 15%.

[40] Pre-tax profits to the year's average value of assets.

II.2. Market Risk

II.2.1. General characteristics of market risk

The number of credit institutions calculating market risk[41] decreased from 790 to 772 in 2005, but their share in banking sector assets expanded from 90.2% to 91.6%.

Banking sector market risk increased 41.5% in the period under review and stood at 371.2 billion rubles as of January 1, 2006. This was mainly due to credit institutions' increased activity on the securities market, reflected in the enlargement of their trade portfolios, and the expansion of credit institutions' operations on derivatives markets. The ratio of market risk to own funds (capital) of banks calculating market risk also increased, from 31.7% to 33.6%. However, the share of market risk in aggregate banking sector risk remained low at less than 5% as of January 1, 2006 *(see Chart 2.3).*

Stock market risk accounted for the largest part of market risk (42.9% as of January 1, 2006), whereas interest rate risk accounted for 39.8% as against 39.8% and 41.8% respectively as of January 1, 2005. At the same time, interest rate risk accounted for the largest part of market risk on some reporting dates during the year due to considerable growth in positions in corporate debt instruments. Overall, the value of corporate debt instruments in the trading book increased 120% in 2005. Foreign exchange risk remained the least important risk (it accounted for 17.4% of aggregate risk as of January 1, 2006 as against 18.3% as of January 1, 2005).

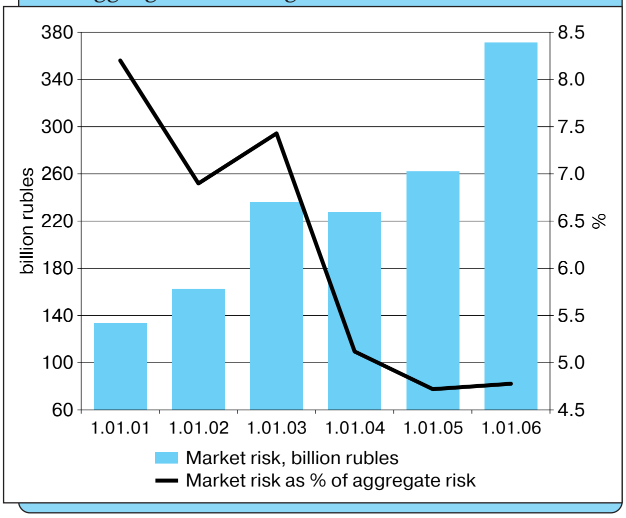
Foreign exchange risk was taken into account in calculating capital adequacy by 677 banks as of January 1, 2006, which accounted for 84.5% of banking sector assets (716 banks accounting for 84.8% of banking sector assets as of January 1, 2005). In comparison, equity position risk was calculated by 138 banks as of January 1, 2006, which accounted for 26% of banking sector assets and interest rate risk was calculated by 252 banks, which accounted for 36% of banking sector assets. The number of banks whose operations are important for all segments of the financial market and which, consequently, must include all the three market risks in the calculation was small at 83 as against 72 as of January 1, 2005. These banks accounted for 21.2% of banking sector assets as of January 1, 2006 (21.9% as of January 1, 2005).

The foreign currency component of banking sector assets and liabilities expanded in 2005 as the nominal rate of the US dollar rose against the ruble on the domestic foreign exchange market *(see Chart 2.4).*

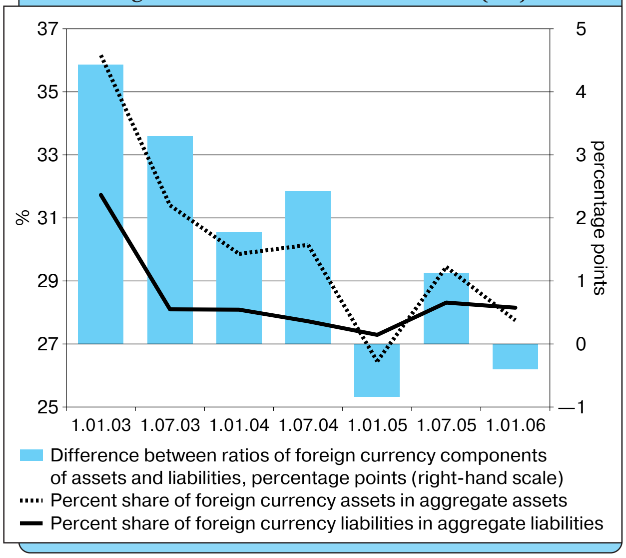
Foreign currency assets accounted for 27.7% of aggregate assets as of January 1, 2006, and foreign currency liabilities accounted for 28.2% of aggregate liabilities (26.5% and 27.3% as of January 1, 2005 respectively). The difference between the ratios of the foreign currency components of assets and liabilities stood at 0.4 percentage points.

The limits set on the open currency positions in 2005 were violated by 13 credit institutions on average per quarter in 2005 (18 credit institutions in 2004). As of Jan-

Market risk and its share in aggregate banking sector risk — *CHART 2.3*



Foreign currency assets and liabilities in aggregate banking sector assets and liabilities (%) — *CHART 2.4*



[41] In compliance with the requirements of Bank of Russia Regulation of September 24, 1999, No. 89-P “On the Procedure for Calculating Market Risks by Credit Institutions”.

uary 1, 2006, banks that violated the limits set on the open currency positions accounted for 14.3% of the assets of the banks holding foreign currency licences (6.6% as of January 1, 2005).

Credit institutions continued to step up their activity on derivative markets in 2005 and this contributed to market risk growth. Claims for the delivery of securities under forward transactions[42] almost doubled in 2005 and obligations increased 60%. The net position (the difference between claims and obligations) on the delivery of securities under forward transactions was negative as of January 1, 2006, at —45.7 billion rubles (in comparison, it was —31.7 billion rubles as of January 1, 2005). Growth in market risk was partly offset by increase in banking sector capital: the net position[43] on the delivery of securities under forward transactions contracts relative to banking sector own funds (capital) remained virtually unchanged in 2005 (3.7% as of January 1, 2006, as against 3.3% as of January 1, 2005).

Credit institutions' currency forward transactions had the following characteristics. The net forward position in US dollars[44] was long as of December 30, 2005, and stood at 6.7 billion rubles as against the net short position of 16.2 billion rubles as of December 31, 2004. The net long forward position in euros stood at 41.3 billion rubles as of December 30, 2005, down 27.6% on the corresponding long position as of December 31, 2004 (57.0 billion rubles). The net option positions in these currencies were considerably smaller: as of December 30, 2005, they stood at 448.0 million rubles in US dollars and 4.9 million rubles in euros.

In 2005, off-balance-sheet foreign currency claims and obligations[45] increased 62.9% and 73.6% respectively. There was also a rise in the ratio between off-balance sheet and balance sheet foreign currency positions. While at the beginning of 2005 the ratio between off-balance sheet claims and balance sheet assets stood at 47.6%, as of January 1, 2006, it was 54.0%. Similar dynamics were registered in the ratio between off-balance sheet claims and balance sheet liabilities in foreign currency, which increased from 40.0% to 49.3% in the period under review.

II.2.2. Evaluation of banking sector vulnerability to foreign exchange risk

To evaluate the Russian banking sector vulnerability to foreign exchange risk, the Bank of Russia stress tested the ruble appreciation against the US dollar and the euro separately. The initial events in the stress situation were one-time sharp rise by 30% in the nominal exchange rates of the ruble against the US dollar and the same rise against euro. To determine the effect of foreign exchange risk on the financial state of the Russian banking sector, it analysed data provided by credit institutions that are required to calculate foreign exchange risk[46] and have net long open positions in the US dollar and the euro.

The number of credit institutions which had net long open positions in the US dollar stood at 402 as of January 1, 2006 as against 326 as of January 1, 2005 and they accounted for 46.0% of aggregate banking sector assets and 44.3% of aggregate banking sector capital (48.5% and 41.4% as of January 1, 2005). The number of credit institutions which had net long open positions in the euro stood at 396 as of January 1, 2006 as against 375 as of January 1, 2005, and their share in aggregate banking sector assets and capital remained virtually unchanged at 25.4% and 30.2% respectively (25.7% and 30.3% as of January 1, 2005).

An analysis shows that by the end of 2005 the long open US dollar positions of the sampled credit institutions had contracted by a third year on year (to $342.1 million) and their share in the long open positions for all foreign currencies and precious metals[47] averaged 71.5% as of January 1, 2006, as against 68.1% as of January 1, 2005. The long open positions in the euro of the sampled credit institutions had increased by a third to $126.2 million and their share in the long open positions for all foreign currencies and precious metals[48] stood at 30.0% on average as of January 1, 2006, as against 26.4% as of January 1, 2005.

The stress test showed that the ruble 30%-appreciation against the US dollar or euro would not cause any significant loss of capital: most banks would lose no more than 3% of their capital.

The stress test also showed that the banking sector vulnerability to a possible sharp rise of the ruble against the US dollar has declined and is low: had the entire scenario materialised, the sampled banks would have lost 0.5% of their capital as of January 1, 2006, as against 1.1% as of January 1, 2005. The banking sector vulnerability to a possible sharp rise of the ruble against the euro is also low: had the entire scenario materialised, the sampled banks would have lost 0.3% of their capital as of January 1, 2006, as against 0.4% as of January 1, 2005.

II.2.3. Evaluation of banking sector vulnerability to interest rate risk (trading book)

To evaluate the banking sector vulnerability to interest rate risk of the trading book, the Bank of Russia conducted a stress test to determine the effect of growth in interest rates on the financial state of the banking sector. It was assumed that as a result of growth in the required

[42] Forward transactions in Section G of the Chart of Accounts.
[43] Regardless of the position sign.
[44] Net forward and option positions in foreign currencies have been calculated according to data in Form 040934 "Open Currency Positions Statement" on all credit institutions presenting this form in ruble terms at the Bank of Russia official exchange rates as of the corresponding dates.
[45] Forward transactions in Section G of the Chart of Accounts.
[46] Foreign exchange risk is taken into account when calculating market risks when as of the reporting date the percent ratio between total open currency positions and own funds (capital) equals or exceeds 2%.
[47] In ruble terms.
[48] In ruble terms.

yield on corporate debt instruments, their price would fall by 30%[49].

To determine the effect of interest rate risk of the trading book on the financial state of the Russian banking sector, the Bank of Russia analysed data reported by credit institutions with positions in resident corporate listed debt instruments in their trading books. For the purposes of the analysis, these credit institutions were divided into two groups: the first group comprised banks required to calculate interest rate risk and, consequently, include market risk in the capital adequacy ratio calculation, the second comprised credit institutions that did not calculate interest rate risk[50].

The number of credit institutions in the first sample increased 43% to 172 as of January 1, 2006, as against 120 as of January 1, 2005. These banks accounted for 54.7% of the value of resident corporate debt instruments in the trading books at the banking sector level. This group of credit institutions accounted for 32.8% of banking sector assets and 32.7% of banking sector capital as of January 1, 2006 (27.5% and 26.6% as of January 1, 2005).

The number of credit institutions in the second sample increased from 76 to 93 in 2005 and accounted for the remaining 45.3% of the value of resident corporate debt instruments in the trading books at the banking sector level. This group of credit institutions accounted for 46.4% of banking sector assets and 39.1% of banking sector capital as of January 1, 2006 as against 46.0% and 35.9% as of January 1, 2005.

The stress testing of the credit institutions ***required to calculate interest rate risk*** showed that overall interest rate risk vulnerability of the tested credit institutions increased in 2005: as of the beginning of this year, their potential loss of capital could be 5.5% as against 4.8% a year earlier.

Interest rate risk vulnerability of credit institutions that have resident corporate listed debt instruments in their trading books but ***do not calculate interest rate risk*** also increased in 2005: had the situation changed for the worse, these credit institutions would have lost 3.8% of their capital (18.5 billion rubles) as of the beginning of this year as against 2.0% (6.8 billion rubles) a year earlier.

Therefore, the expansion of the credit institutions' trading books led to the banking sector becoming more vulnerable to interest rate risk. It should be noted that if the proposed scenario had materialised, some banks would have incurred heavy losses.

II.2.4. Evaluation of banking sector vulnerability to equity position risk

To assess the financial stability of the Russian banking sector against equity position risk by stress testing, the Bank of Russia evaluated the possible negative consequences of a fall in the RTS index. It assumed as the initial event in the stress situation the decline of the RTS index by 30%[51].

To determine the effect of equity position risk on the banking sector capitalisation, the Bank of Russia analysed data reported by credit institutions that had listed stocks in their trading books. As was the case with the analysis of interest rate risk, credit institutions were divided into two groups: the first included banks that were required to calculate equity position risk and, consequently, include it in the capital adequacy ratio calculation, and the second comprised credit institutions that did not calculate equity position risk.

The number of credit institutions in the first group increased from 111 to 134 and as of January 1, 2006, they accounted for 75.9% of the value of listed stocks in the trading books at the banking sector level. This group of credit institutions accounted for 26.0% of banking sector assets and 27.6% of banking sector capital as of January 1, 2006 as against 24.9% and 24.7% as of January 1, 2005.

The number of credit institutions in the second group fell from 156 to 125 and as of January 1, 2006, they accounted for the remaining 24.1% of the value of listed stocks in the trading books at the banking sector level. This group of credit institutions accounted for 45.8% of banking sector assets and 38.7% of banking sector capital as of January 1, 2006 as against 47.8% and 39.2% as of January 1, 2005.

An analysis showed that in the group of credit institutions ***calculating equity position risk*** a 30% fall in the RTS index would not cause serious losses: as of the beginning of this year they would have accounted for 4.3% of capital as against 3.8% a year earlier.

In the group of credit institutions that have listed stocks in their trading books but ***do not calculate equity position risk,*** vulnerability to equity position risk remained virtually unchanged: had the situation taken a bad turn, their losses would have accounted for 1.0% of capital as of the beginning of 2006 as against 1.1% a year earlier.

Overall, the stress test showed that the banking sector vulnerability to equity position risk, evaluated as a possible sharp fall in the RTS index, is relatively low.

[49] Depreciation of investments in government securities was not evaluated due to, first, the raising of Russia's sovereign credit rating to the investment grade by leading international rating agencies and, second, the high concentration of the federal loan bond (OFZ) market, on which the principal players are, as before, Sberbank and the Pension Fund of the Russian Federation (as of January 1, 2006, Sberbank accounted for 62.3% of aggregate banking sector investments in government debt instruments).

[50] Bank of Russia Regulation of September 24, 1999, No. 89-P "On the Procedure for Calculating Market Risks by Credit Institutions", requires interest rate and stock market risks to be also calculated when the total balance sheet value of the trade portfolio equals or exceeds 5% of the credit institution's balance sheet assets as of the reporting date. The total balance sheet value of the trade portfolio is determined as the sum of the balance sheet values of the financial instruments that have market value and have been acquired by the credit institution for subsequent resale, repo-type instruments included.

[51] It was assumed that the RTS index's fall by 30% would lead to the same decrease in shares' prices in trade portfolios.

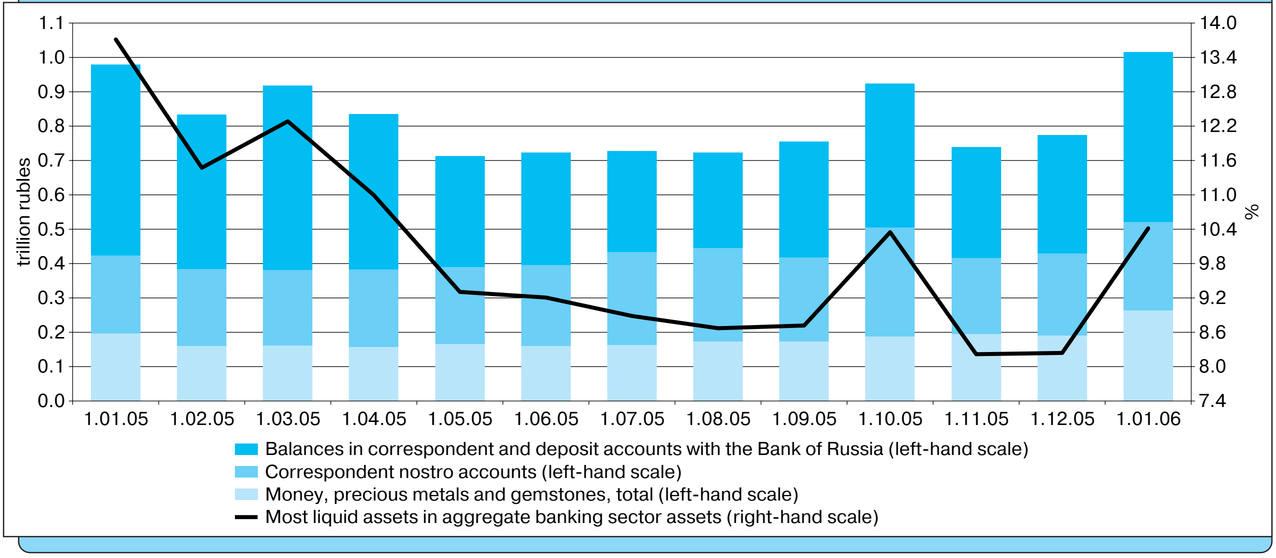
II.3. Liquidity Risk

II.3.1. Dynamics of most liquid assets

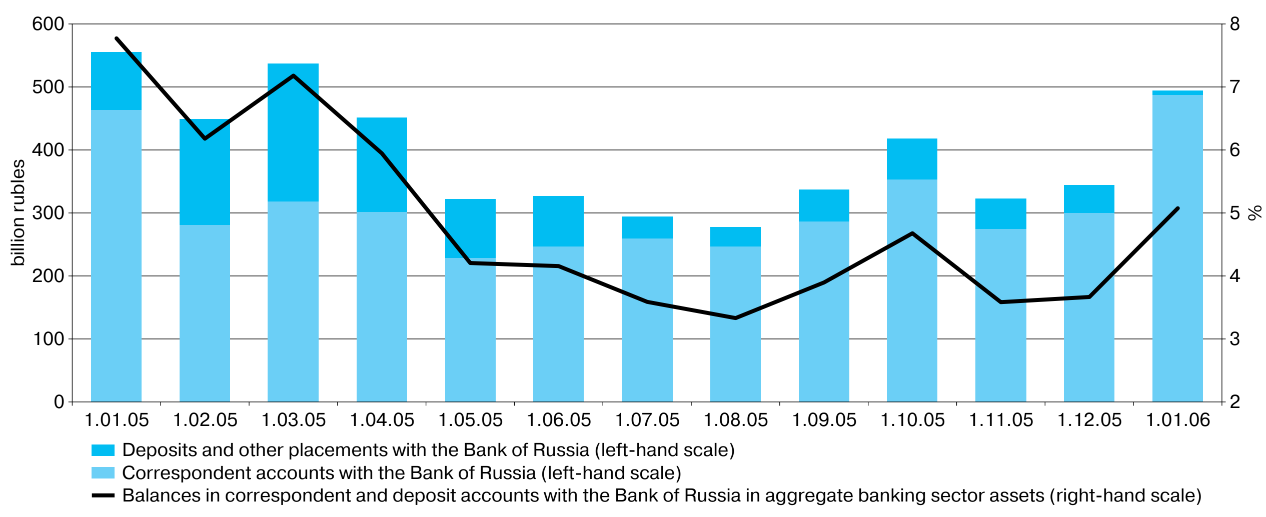
The banking sector most liquid assets (money, precious metals and gemstones, balances in correspondent nostro accounts and balances in correspondent and deposit accounts with the Bank of Russia) increased slightly in 2005 (by 3.8%) and totalled 1,015.7 billion rubles as of January 1, 2006. However, there was marked contraction in the share of the most liquid assets in aggregate banking sector assets, from 13.7% to 10.4% *(see Chart 2.5)*. These dynamics of the most liquid assets were due to the expansion of the share of higher-yielding assets in banks' balance sheets, which slightly increased liquidity risk.

The value of funds in correspondent nostro accounts increased 13.0% in 2005, of which the balances in correspondent nostro accounts in resident credit institutions rose 2.3% and the balances in correspondent nostro accounts in non-resident banks grew 19.6%.

Banking sector most liquid assets *CHART 2.5*



Balances in credit institutions' correspondent and deposit accounts with Bank of Russia *CHART 2.6*



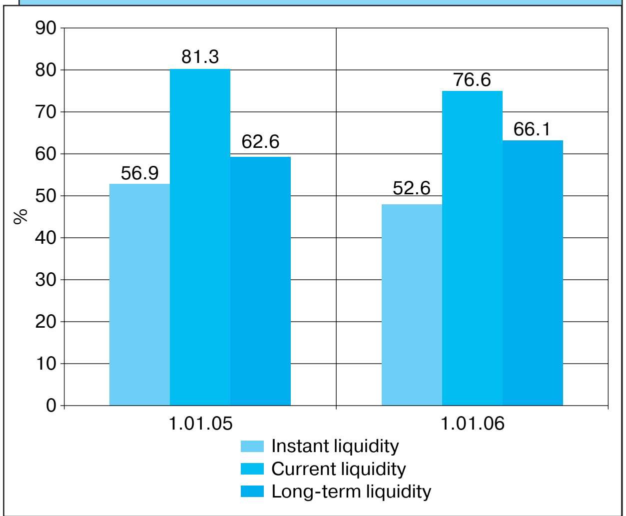
The balances of credit institutions' correspondent and deposit accounts with the Bank of Russia had declined throughout 2005 and as of January 1, 2006, they accounted for 5.1% of aggregate banking sector assets as against 7.8% as of the beginning of last year *(see Chart 2.6).*

Most of the groups of banks registered a contraction in the share of the most liquid items in aggregate assets. The only exception was the medium-sized and small banks based in the Moscow Region, which registered an increase in the share of the most liquid assets in the group's aggregate assets. These banks also registered an increase in the share of funds in their correspondent and deposit accounts with the Bank of Russia.

II.3.2. Compliance with required liquidity ratios

There were few cases in 2005 when some credit institutions failed to comply with required liquidity ratios[52] and the number of credit institutions failing to comply with the instant liquidity ratio declined (four credit institutions as of January 1, 2005, three as of April 1, 2005, three as of July 1, 2005, and one as of October 1, 2005). The same was true of the current liquidity ratio (four credit institutions as of January 1, 2005, three as of April 1, 2005, one as of July 1, 2005, and one as of October 1, 2005), and the long-term liquidity ratio (two credit institutions as of April 1, 2005, and one as of July 1, 2005). As of January 1, 2006, all credit institutions complied with the required liquidity ratios.

Banking sector liquidity ratios (chronological annual averages) *CHART 2.7*



In 2005, all credit institutions, which were among the top 20 banks in terms of assets, complied with the instant (N2), current (N3) and long-term liquidity (N3) ratios. The banking sector's average annual chronological liquidity ratios decreased slightly: the instant liquidity ratio fell from 56.9% in 2004 to 52.6% in 2005 and the current liquidity ratio was down from 81.3% to 76.6% *(see Chart 2.7).*

As of January 1, 2006, the banking sector instant and current liquidity ratios stood at 54.7% and 73.8% respectively.

The smallest instant liquidity ratio (51.9%) at the end of 2005 was registered in the group of diversified banks. State-controlled banks and intra-group banks had smaller instant liquidity ratios than the banking sector average (53.1% and 53.9% respectively).

The smallest current liquidity ratio (66.5%) was registered in the banks controlled by foreign capital. State-controlled banks also had a smaller current liquidity ratio than the banking sector average (67.0%).

The average long-term liquidity ratio[53] rose slightly (from 62.6% as of January 1, 2005, to 66.1% as of January 1, 2006). The relatively small increase resulted from the fact that though growth in banking sector liabilities with maturities longer than one year (by 63.2%) exceeded growth in long-term lending (by 1.9 percentage points), the expansion of long-term (longer than one year) lending operations (by 61.4%) exceeded growth in banking sector capitalisation by two times (aggregate banking sector capital increased 31.2%).

Despite a slight contraction in the share of the most liquid assets in aggregate banking sector assets and the reduction of the banking sector instant and current liquidity ratios, overall banking sector liquidity was at an acceptable level in 2005. The dynamics of the following indicators bear this out: the structure of banking sector assets and liabilities by maturity, the cover ratio, interbank market rates and the ratio reflecting credit institutions' dependence on the interbank market.

II.3.3. Structure of banking sector assets and liabilities by maturity[54]

The maturity period of the aggregate banking sector loan portfolio increased in 2005. The value of loans with original maturities longer than one year continued to grow faster than total loan debt[55] (60.4% as against 40.0%). (In 2004, funds provided for terms longer than one year increased 53.8% and total loan debt grew 44.6%).

As a result, the share of medium- and long-term (over one year) component of the loan portfolio continued to expand: as of January 1, 2006, it stood at 49.7% of total

[52] Bank of Russia Instruction of January 16, 2004, No. 110-I "On Banks Prudential Ratios" defines a failure to comply with the required liquidity ratio as the violation of its numerical value for a total of six business days or more within any 30 consecutive business days.
[53] Bank of Russia Instruction of January 16, 2004, No. 110-I "On Banks Prudential Ratios" sets the maximum long-term liquidity ratio at 120%.
[54] Banking sector assets and liabilities by maturity were analysed on the basis of data on the distribution of balance sheet assets and liabilities by term.
[55] Loan debt includes loans extended by credit institutions to legal entities and households, except resident banks and financial institutions, and other funds provided to these categories of resident and non-resident debtors.

loan debt as against 43.4% as of January 1, 2005. At the same time, the share of short-term loan debt contracted, of which the loan debt of up to 30 days decreased from 7.8% as of January 1, 2005, to 6.4% as of January 1, 2006 *(see Chart 2.8).*

Similar changes were registered in the structure of deposits[56] taken by credit institutions. In 2005, deposits with original maturities longer than one year grew faster (by 57.2%) than total deposits (by 50.7%). Deposits with original maturities longer than one year accounted for 54.9% of total deposits as of January 1, 2006, as against 52.7% as of January 1, 2005. At the same time, there was a slight increase in the share of deposits with original maturities shorter than 30 days (from 14.5% as of January 1, 2005, to 15.6% as of January 1, 2006).

All groups of credit institutions registered an increase in the share of the medium- and long-term components of credit investments and deposits taken.

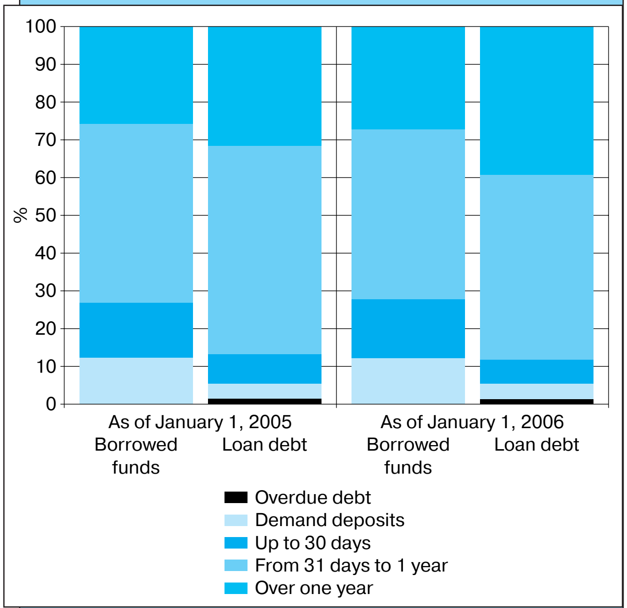
State-controlled banks had the longest-term structure of deposits taken and loan debt: the share of customer deposits with original maturities longer than one year stood at 69.3% of total deposits taken and the share of loans extended for the same term was 60.0%.

In all other groups of credit institutions the long-term component of customer deposits and loans extended to clients was smaller than the banking sector average.

Banks with foreign interest had the smallest share of customer deposits with original maturities longer than one year: about a half of customer deposits were taken for less than 30 days.

The smallest share of loans with original maturities longer than one year was registered in the group of medium-sized and small banks based in the Moscow Region (31.0%). Nearly half of all loans were extended by banks in this group for a term of 30 days to one year.

Structure of loan debt and borrowed funds by maturity CHART 2.8



Customer deposits to total loans (the cover ratio)[57]

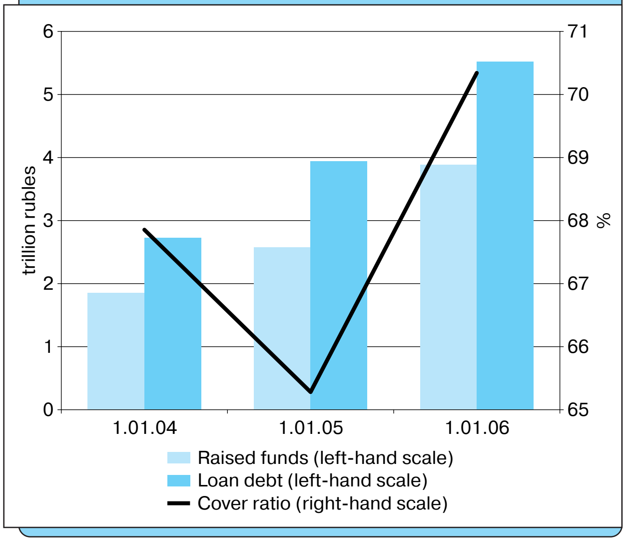
The 2004 trend towards reducing the cover ratio changed in 2005 and as of January 1, 2006, customer deposits covered 70.2% of loans extended to customers, which represents a slight increase on the cover ratio registered as of January 1, 2005 (65.2% as against 68.0% as of January 1, 2004 *(see Chart 2.9).*

Ninety-five credit institutions had no corporate or household deposits as sources of their resources, but these credit institutions accounted for a meagre 1.0% of aggregate banking sector assets.

The highest cover ratio (82.2%) was registered in state-controlled banks as of January 1, 2006.

The lowest (43.8%) was in the group of medium-sized and small banks based in the Moscow Region.

Loan debt to main sources of banking sector financing CHART 2.9



[56] These include deposits taken by credit institutions from legal entities and households, except resident banks and financial institutions, and other funds raised from these categories of resident and non-resident creditors, excluding balances in current and settlement accounts of these categories of clients.

[57] The cover ratio is calculated as the ratio of loans extended by credit institutions to legal entities and households, except resident banks and financial organisations, and other funds provided to these categories of resident and non-resident debtors to deposits taken by credit institutions from resident and non-resident legal entities and households, except resident banks and financial institutions, and other funds raised from these categories of resident and non-resident creditors, excluding the balances of current and settlement accounts of these categories of customers.

Calculation of this indicator (“Customer deposits to total (non-interbank) loans”) is recommended by the IMF for the analysis of financial stability in the “Compilation Guide on Financial Soundness Indicators”. This indicator allows one to evaluate banking sector liquidity, as it compares the most “traditional” and stable sources of resources with their principal investments. The reduction of the cover ratio is indicative of the increased dependence of the fulfilment of credit institutions’ obligations on their ability to access the money or stock market quickly and, consequently, the increased liquidity risk.

II.3.4. Fulfilment of obligations

There were few cases in 2005 when credit institutions failed to meet their obligations to creditors and depositors (one credit institution as of January 1, 2005, three credit institutions as of April 1, 2005, one credit institution as of July 1, 2005, and two credit institutions as of October 1, 2005). These credit institutions accounted for a small part of aggregate banking sector assets (no more than 0.5%).

The ratio of credit institutions' unsatisfied claims and compulsory payments to their total liabilities had contracted from 0.4% as of January 1, 2005, to nought by the end of last year.

There were no cases of non-fulfilment by credit institutions of their obligations to creditors and depositors as of January 1, 2006.

II.3.5. Dependence on interbank market[58]

Credit institutions' dependence on the interbank market decreased slightly in 2005. The following data bear this out.

Credit institutions with a PL5 ratio of not more than 8% accounted for the largest part of aggregate banking sector assets and in 2005 their share expanded from 65.5% to 71.2%. The share of credit institutions with a PL5 ratio from 8% to 18% contracted from 19.0% to 12.4% of banking sector assets. The share of credit institutions with a PL5 ratio of 18% to 27% stood at 10.6% as of January 1, 2006 (as against 9.7% as of January 1, 2005) and the share of credit institutions with a PL5 ratio in excess of 27% remained unchanged at 5.8%.

Banks with foreign interest registered the highest interbank market dependence ratio (19.9%) as of January 1, 2006, which is attributable to their active co-operation with their foreign-based parent banking structures. Banks from this group with a PL5 ratio in excess of 18% accounted for 52.5% of this group's assets.

Medium-sized and small banks based in the Moscow Region were the least dependent on the interbank market (—2.3%).

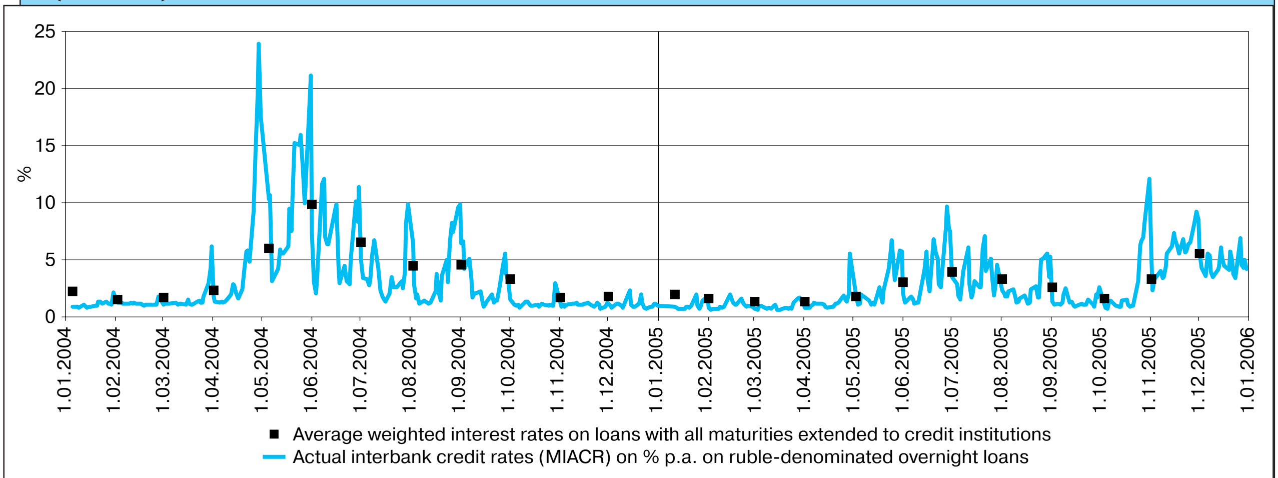
The interbank lending market has a major role to play from the standpoint of liquidity management. Non-resident banks exert a significant influence on Russia's interbank lending market. In the past few years, Russian banks have raised more funds on the interbank market (784.0 billion rubles as of January 1, 2006, as against 514.2 billion rubles a year earlier) than they have placed on it (351.7 billion rubles as against 196.0 billion rubles respectively).

However, the following tendency seems important from the standpoint of the Russian banking sector long-term development: the share of non-resident banks has been gradually expanding in interbank loans, both taken and placed. In 2005, the share of loans received from non-resident banks in total interbank loans received increased by 2.4 percentage points to 72.2%, whereas the share of loans extended to non-resident banks in total interbank loans expanded by 6.6 percentage points to 52.7%.

The excess of interbank loans received from non-resident banks over loans extended to these banks in Russian banking sector liabilities remained virtually unchanged at 4.4% in 2005.

Nearly 200 Russian banks, accounting for about 83.8% of aggregate banking sector assets, conducted operations on the international interbank market in 2005. Six banks from the group of the largest 20

Ruble interbank credit rates (MIACR) *CHART 2.10*



[58] The ratio of credit institutions' dependence on the interbank market (PL5 ratio) is calculated in compliance with Bank of Russia Ordinance of January 16, 2004, No. 1379-U "On the Evaluation of Financial Soundness of a Bank for the Purpose of Ascertaining its Sufficiency for Participation in the Deposit Insurance System", as a percent difference between the interbank loans (deposits) taken and placed and the funds raised. The Ordinance sets the threshold ratios from 8% to 27% and more. The higher the ratio, the more the credit institution depends on the interbank market.

banks in terms of assets (most of them were the top Russian banks from the group of state-controlled and diversified banks and banks controlled by foreign capital) accounted for a half of the value of interbank loans received from non-resident banks and placed with these banks.

As of January 1, 2006, 20 banks (18 banks as of January 1, 2005), most of which were among the top largest banks by assets, accounted for almost 80% of total loans received from non-resident banks.

As of January 1, 2006, 22 banks (20 banks as of January 1, 2005), most of which were among the 50 largest banks by assets and half of which were among the top 20 banks, accounted for 80% of total loans placed with non-resident banks.

II.3.6. Interbank market interest rates

The Moscow Interbank Actual Credit Rate (MIACR) on ruble-denominated overnight loans, the best indicator of the current price of the ruble resources on the interbank market, was lower in 2005 than in 2004.

The MIACR dynamics of interbank loans with maturities from two to seven days and from eight to 30 days followed the MIACR dynamics of overnight loans. The occasional surges of interest rates on the ruble interbank market in 2005 occurred mostly when tax payments were made to the budgets of all levels *(see Chart 2.10).*

The annual average weighted interest rate on interbank loans with all maturities stood at 3.1% in 2005, down by 0.9 percentage points on 2004.

II.4. Capital Adequacy

II.4.1. Banking sector own funds (capital) dynamics and structure

Banking sector own funds (capital) amounted to 1,241.8 billion rubles as of January 1, 2006. In 2005, it grew almost twice as fast as in 2004 (by 31.2% as against 16.2%). As a result, the ratio of banking sector capital to GDP rose slightly (from 5.6% as of January 1, 2005, to 5.7% as of January 1, 2006). At the same time, banking sector capital to assets contracted to 12.7%, whereas in the previous years it had varied between 14.6% and 13.3% *(see Chart 2.11).*

Growth in regulatory capital was registered in 2005 by 1,110 credit institutions, or 88.6% of the total number of operating credit institutions, an increase of 66, or by 8.2 percentage points, on the previous year.

Credit institutions' profits remain a major source of banking sector capitalisation. Overall, growth in banking sector regulatory capital in 2005 was due to an increase of 147.2 billion rubles in profits and funds created from them (this accounts for a half of total regulatory capital growth).

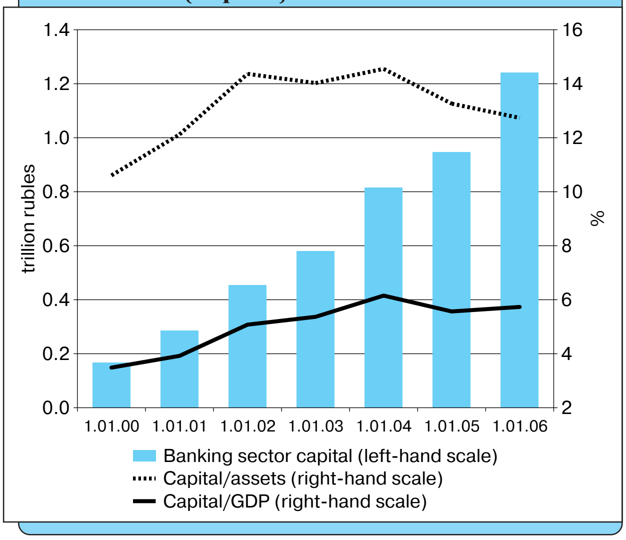
The second most important factor of growth in banking sector capital last year was a year-on-year increase of 101.0 billion rubles in subordinated loans taken, which accounted for 34.2% of total regulatory capital growth. A year earlier subordinated loans were the third most important factor of growth in aggregate banking sector capital. This source of capitalisation was mostly used by large Russian banks with high international ratings, which enabled them to raise credit on international financial markets (it should be noted that the procedure for raising subordinated debt is less regulated organisationally and legally than an IPO, for example).

The paid-up authorised capital of operating credit institutions as a factor of growth in aggregate banking sector capital in 2005 moved from the second to the third place, increasing by 67.3 billion rubles and accounting for 22.8% of total regulatory capital growth.

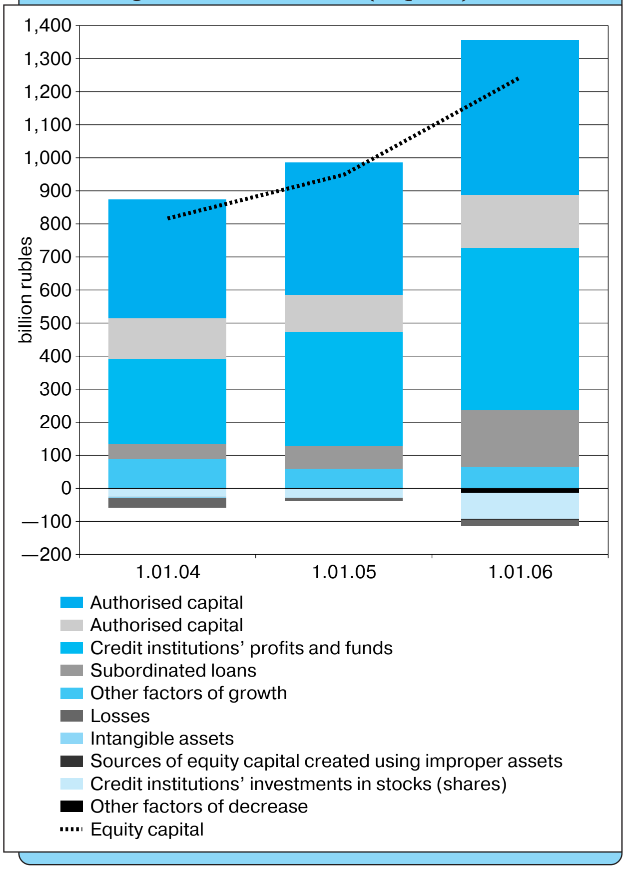
At the same time, the share of authorised capital in regulatory capital continues to contract: it decreased from 42.2% in 2004 to 37.6% in 2005 as against 53.5% in 2002 and 44.0% in 2003. The share of subordinated loans expanded by 90% to 13.7%, because several large banks gained access to the subordinated loan market in 2005 *(see Chart 2.12).*

Profits and the funds created from them accounted for 39.6% of aggregate banking sector capital in 2005 as against 36.4% in 2004. Subordinated loans taken by banks in compliance with the capital requirements[59] enable them to increase their regulatory capital and meet

Banking sector own funds (capital) *CHART 2.11*



Structure of aggregate banking sector own funds (capital) *CHART 2.12*



[59] In accordance with point 3.11.1 of Bank of Russia Regulation of February 10, 2003, No. 215-P "On the Methodology for Determining Own Funds (Capital) of Credit Institutions", the value of a subordinated loan, included in the sources of supplementary (Tier II) capital, must not exceed 50% of main (Tier I) capital.

the capital adequacy requirements. In addition, subordinated loans allow banks to expand the range of investors without reducing the share of the bank's present owners in capital.

The importance of regulatory capital growth factors differs significantly for different groups of credit institutions.

In the group of state-controlled banks, for example, the increase in own funds (capital) was largely due to the taking of subordinated loans, which accounted for 36.3% of the capital growth factors and the capitalisation of profits and the funds created from them (35.6%). The high level of efficiency of the state-controlled banks and low level of risk inherent in their business make the extension of subordinated loans to them an attractive instrument for foreign investors.

The intra-group banks built up their regulatory capital mainly by capitalising profits (71.7% of total growth).

As for the diversified banks, the capitalisation of profits accounted for 39.8% of total growth in their regulatory capital, the increase in authorised capital accounted for 30.1% and the taking of subordinated loans 20.3%.

The main factor of growth in regulatory capital in the banks controlled by foreign capital (53.2% of total growth) was the increase in authorised capital. The second most important factor of growth in regulatory capital in this group of banks was the capitalisation of profits and the funds created from them (30.7%). The same factors of capitalisation growth predominated in the group of medium-sized and small banks based in the Moscow Region (59.3% and 40.5%) and the group of medium-sized and small regional banks (38.2% and 38.0%).

In 2005, 134 credit institutions registered a contraction in regulatory capital by a total of 10.8 billion rubles (244 credit institutions by 7.2 billion rubles in 2004). These credit institutions accounted for 3.9% of banking sector assets as of January 1, 2006 as against 9.5% as of January 1, 2005. Capital reduction was registered mostly in intra-group banks (6.4 billion rubles), whose share in the group's total capital stood at 17.2% and in aggregate banking sector capital 3.3%.

As was the case a year earlier, there were no credit institutions with negative own funds (capital) as of January 1, 2006 (as of January 1, 2004, there was one credit institution with negative capital and as of January 1, 2003, there were two).

II.4.2. Compliance with the capital adequacy requirement

The gradual decline in the banking sector's average capital adequacy ratio is continuing as growth in aggregate banking sector assets exceeds growth in aggregate banking sector own funds (capital) and risk increases. In 2005, the capital adequacy ratio decreased from 17.0% to 16.0% *(see Chart 2.13).*

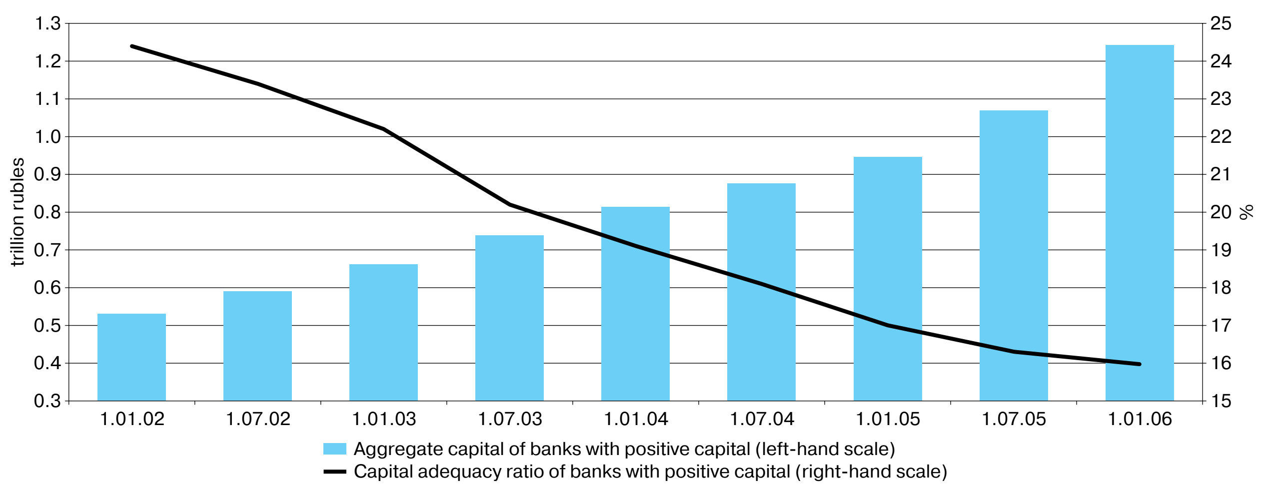
Risk-weighted banking sector assets increased 39.8% in 2005 year on year and banking sector capital expanded 31.2% over the same period.

All groups of banks, except the state-controlled ones, registered a fall in the capital adequacy ratio in 2005. At the same time, the medium-sized and small banks based in the Moscow Region had the highest capital adequacy ratio (32.9%). Higher capital adequacy ratios than the banking sector average were registered as of January 1, 2006, in the group of medium-sized and small regional banks (22.4%), banks controlled by foreign capital (19.0% and intra-group banks (18.9%).

As was the case a year earlier, only one credit institution failed to comply with the capital adequacy ratio (N1) as of January 1, 2006[60].

Capital adequacy ratio

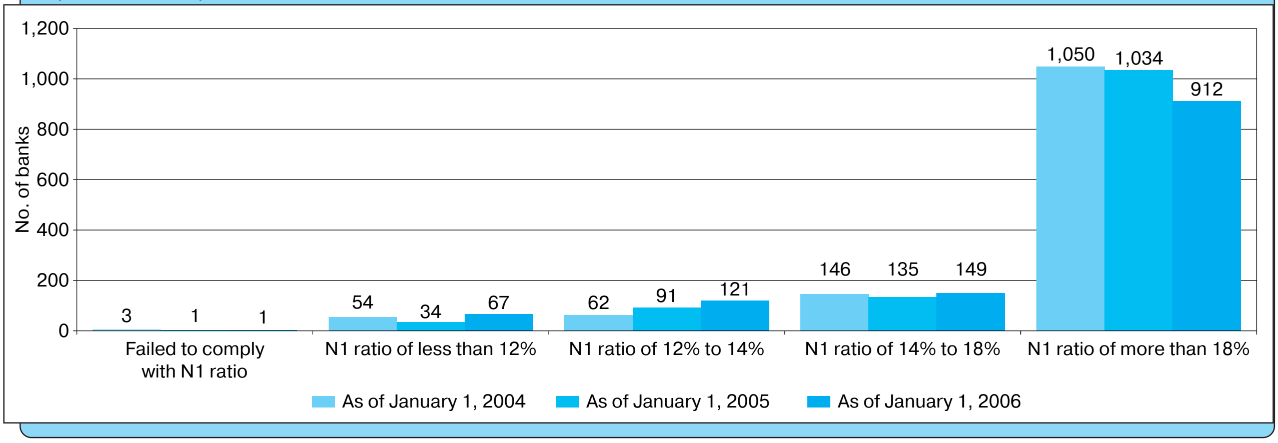
CHART 2.13



[60] Bank of Russia Instruction of January 16, 2004, No. 110-I "On Banks Prudential Ratios", defines non-compliance with the N1 ratio as the failure to comply with it for a total of six business days and more within 30 consecutive business days preceding the reporting date.

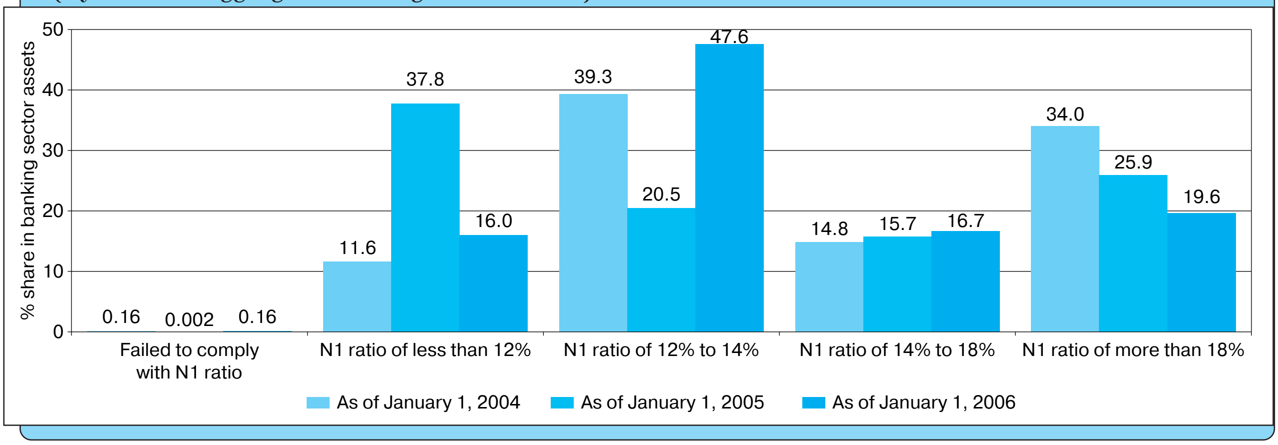
Credit institutions grouped by capital adequacy ratio (by number)

CHART 2.14



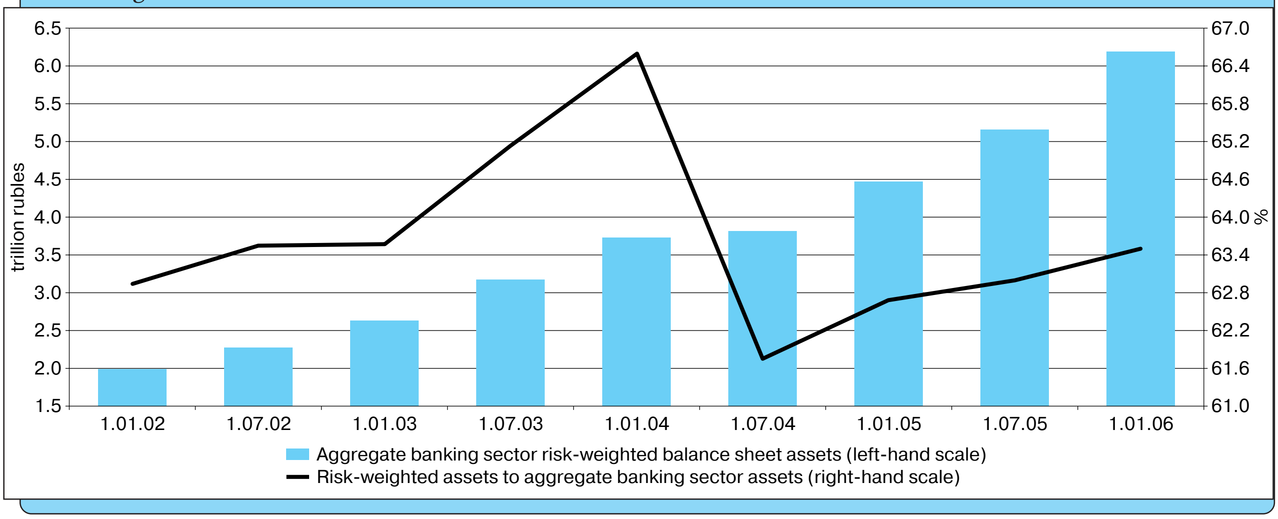
Credit institutions grouped by capital adequacy ratio (by share in aggregate banking sector assets)

CHART 2.15



Risk-weighted banking sector assets

CHART 2.16



The distribution of credit institutions by capital adequacy ratio improved on the whole in 2005. The share of credit institutions with a capital adequacy ratio of less than 12% decreased by more than half (from 37.8% to 16.0%). Credit institutions with a capital adequacy ratio in the range of from 12.0% to 14.0% account for nearly a half of aggregate banking sector assets, whereas their share in assets expanded from 20.5% to 47.6%. Credit institutions with a capital adequacy ratio of more than 14.0% remain the largest group, but their share in aggregate banking sector assets contracted from 41.7% to 36.3% in 2005 *(see Chart 2.14 and Chart 2.15).*

The capital adequacy ratio of the 20 largest banks by assets stood at 13.2% as of January 1, 2006 as against 13.0% as of January 1, 2005.

II.4.3. Evaluation of risk-weighted assets

The ratio of risk-weighted balance sheet assets of credit institutions to aggregate assets increased slightly in 2005, from 62.7% to 63.5% *(see Chart 2.16).*

The structure of risk-weighted balance sheet assets in 2005 remained virtually unchanged on 2004. As of January 1, 2006, assets in 1—3 risk groups accounted for 3.0% and assets in 4—5 risk groups 97.0% of risk-weighted balance sheet assets.

Last year's growth in aggregate risks (by 39.8%) was chiefly due to the increase in credit risk from balance sheet assets[61], which accounted for 84.3% of growth in this risk. The structure of aggregate risks did not change significantly in 2005: credit risk continued to predominate. As of January 1, 2006, credit risk from balance sheet assets accounted for 79.7% of aggregate risks (as against 80.5% as of January 1, 2005), credit risk on contingent liabilities of credit nature 9.7% (as against 9.4% as of January 1, 2005), credit risk from forward transactions 0.5% (as against 0.6% as of January 1, 2005) and market risk 4.8% (as against 4.7% as of January 1, 2005).

Credit risk predominated in the structure of aggregate risks in all groups of banks. As of January 1, 2006, the highest level of market risk (9.3%) was registered in the intra-group banks and the highest level of credit risk on below-line balance account assets (15.0%) in the banks controlled by foreign capital.

[61] Taking into account credit institutions' credit risks from claims on the counterparty with regard to the reverse (forward) part of transactions, which arose as a result of the acquisition of financial assets with the simultaneous assumption of obligations for their reverse alienation and claims on persons affiliated with the bank.

II.5. Bank Management Quality

Many credit institutions sought to upgrade their banking risk management techniques in 2005. On the positive side of credit institutions' management, the absence of any significant negative trends in the dynamics of the banking sector's financial performance indicators last year should be noted.

The improvements in the organisation of internal controls included the continued raising of the qualification levels of the internal control services staff and the upgrading of the methods used by credit institutions to ensure independence of their internal controls from the executive bodies and divisions under control.

At the same time, some problems remained unresolved, most of which were connected with shortcomings in corporate governance.

Specifically, the relations between credit institutions and affiliated parties remained imperfectly transparent as, on the one hand, the law does not require affiliated parties to disclose information to credit institutions about themselves and their activities, business reputation and financial state and, on the other hand, some credit institutions only went through the necessary procedures without really trying to identify such parties or disclose information about them.

Many credit institutions retained an incoherent and inefficient system of separation of powers between the various management bodies, which usually led to unjustified interference in the activities of credit institutions by affiliated parties, excessive involvement of their boards of directors (supervisory boards) in the day-to-day management of banks, while matters of strategic importance and the objective assessment of the credit institutions' performance were neglected. On the other hand, the executive bodies were deprived of the necessary powers to perform their functions and bore no responsibility for the results of their work.

Flaws in the structure of the boards of directors (supervisory boards) formed by banks were quite common. A board of directors (supervisory board) may have the wrong number of members or its members may not have the necessary qualifications to pass fair judgements regardless of the opinion of the bank's management or owners.

Despite the concerted efforts made by the Bank of Russia and Federal Antimonopoly Service to ensure that credit institutions disclose information on the real cost of the banking services they provide to their customers, especially consumer lending, banks' policies in this area leave much to be desired.

II.6. Stress Testing the Banking Sector

To evaluate the soundness of credit institutions against economic shocks, the Bank of Russia conducted a stress test of the Russian banking sector[62], which was based on data reported by the 200 largest banks by assets. These banks accounted for 89.2% of aggregate banking sector assets and 83.8% of own funds (capital) as of January 1, 2006. The slowing or termination of economic growth, which may be caused by a fall in oil prices, was selected as the initial event that triggered the stress situation.

Two possible courses of events, or a conservative and pessimistic scenario[63], were considered for the purposes of the stress test. On the whole, it was assumed that the situation would have the following negative consequences:

— an expansion of the share of non-performing loans[64] in banks' loan portfolio and uncollectible loans extended to non-financial corporations and households;
— a run on household and corporate bank deposits;
— depreciation of banks' liquid assets, including the securities trade portfolio;
— losses incurred by banks whose foreign currency liabilities exceeded foreign currency assets.

The stress test showed that total losses may stand at 1.8% of GDP in the baseline scenario and 2.9% of GDP in the worst-case scenario (1.7% and 2.6% in 2004). According to the stress test results, growth in possible losses was caused in 2005, as compared with 2004, mostly by significantly expanded banking operations, accompanied by the accumulated risks in the banking sector.

The calculations showed that credit risk was the most significant for the Russian banking sector. It may cause losses of 30.2% of capital in the baseline scenario and 43.9% in the worst-case scenario.

The risk of lending to the sector of non-financial corporations is the biggest credit risk, accounting for more than 90% of aggregate losses from credit risk in the baseline and worst-case scenarios.

Possible losses on loans to households, calculated in the course of the stress test, are relatively small. Only one credit institution in the baseline scenario and seven in the worst-case scenario may lose more than 50% of capital from this risk. These seven credit institutions account for a little over 2% of banking sector assets and capital. However, rapid growth in the risk of lending to households should be remembered. Potential losses from this risk in 2005 increased both in absolute terms and relative to capital.

The potential losses of credit institutions from market risk does not seem dangerous for the systemic stability of the banking sector, varying between 0.4% of GDP in the baseline scenario and 0.6% of GDP in the worst-case scenario.

At the same time, losses from interest rate risk accounted for the largest part of market risk, but losses from foreign exchange and equity position risks seem relatively small.

The liquidity risk calculated in the course of stress testing does not pose a serious threat to banking sector stability either. Credit institutions' losses from liquidity risk are estimated at less than 0.14% of GDP in both scenarios. At the same time, other risks, especially credit risk, may affect problems associated with the display of liquidity risk.

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[62] The stress testing methodology used before has been changed. Specifically, it now includes the calculation of risk involved in lending to households, an allowance has been made for a possible run on corporate deposits in the methodology of calculating liquidity risk and some ratios have been revised.

[63] The baseline and worst-case scenarios differed in the force of the projected shock, which was reflected in the ratios used in the formulas employed in calculating its after-effects.

[64] For the purposes of the stress test, non-performing loans denote problem and bad loans in accordance with the classification established in Bank of Russia Regulation No. 254-P "On the Procedure for Making by Credit Institutions Loan Loss Provisions, Provisions for Loan Debts and Similar Debts". Before August 1, 2004, non-performing loans denoted doubtful and bad loans as they were defined in Bank of Russia Regulation of June 30, 1997, No. 62a "On the Procedure for Making and Using Loan Loss Provisions", which used different loan classification principles. The effect of this factor on loss levels is relatively small, but it has to be taken into account when interpreting the stress test results.

Banking Regulation and Supervision in Russia

III

III.1. General Characteristics of Banking Regulation and Supervision

III.1.1. Bank of Russia tasks in banking regulation and supervision

The principal objectives of the Bank of Russia as the banking regulation and supervision authority under the Federal Law "On the Central Bank of the Russian Federation (Bank of Russia)" are to maintain the Russian banking system's stability and protect the interests of depositors and creditors.

The main medium-term tasks for the Bank of Russia in upgrading banking regulation and supervision are described in detail in the joint policy document of the Russian Government and the Bank of Russia, entitled *The Russian Banking Sector Development Strategy until 2008* (hereinafter referred to as the Strategy).

Monetary Policy Guidelines for the year 2005 set the following tasks for the Bank of Russia in upgrading banking supervision:

— completing, on the whole, the establishment of the deposit insurance system;
— encouraging the use of substantive supervision, particularly increasing the accuracy of assessment of credit institutions' financial soundness and using, whenever necessary, the appropriate supervisory measures and responding to latent financial problems in credit institutions as soon as they are detected, including the timely requirements to implement financial rehabilitation;
— improving prudential reporting by credit institutions, including the use of advanced information technologies for presenting statements to the Bank of Russia in electronic form alone and upgrading the methodology of verifying reported data;
— using IFRS statements in analysing credit institutions' activities in the course of supervision;
— ensuring greater transparency of the ownership structure of credit institutions;
— establishing additional requirements to prevent managers and owners with a dubious reputation and unsound financial position from infiltrating the management of credit institutions;
— upgrading credit institution liquidation procedures by creating an effective mechanism to sell the assets of liquidated banks, accelerating bank liquidation procedures and making them more efficient, preventing fictitious bank bankruptcies and protecting the interests of creditors and depositors, ensuring the transparency of the receivers' (liquidators') actions, ensuring the accountability of persons responsible for bringing a credit institution to bankruptcy and detecting and disputing dubious transactions conducted shortly before bankruptcy;
— simplifying bank reorganisation procedures;
— giving credit institutions wider powers to create internal structures to expand their networks by establishing new kinds of internal structures in credit institutions and their branches, and creating a favourable environment for access to banking services in Russia's regions;
— continuing vigorous efforts to supervise credit institutions' compliance with the requirements of the Federal Law "On Countering the Legalisation (Laundering) of Criminally Obtained Incomes and the Financing of Terrorism", including the withdrawal from the banking services market of credit institutions in gross violation of the standards of applicable legislation;
— beginning, in collaboration with the banking community, to prepare for the introduction of international capital adequacy standards established by the Basel New Capital Accord (Basel II) by studying the nature and scale of the changes that must be made to laws and regulations in connection with the introduction of these standards.

III.1.2. Bank of Russia supervisory staff

The Bank of Russia supervisory divisions have a staff of 4,324 executives and experts, of whom 12.9% work in the head office and 87.1% in regional branches. Most of the experts have a specialised higher education (95.8%); 81.5% are under 50 and 91.6% have worked in the banking system for three years or more.

In 2005, the Bank of Russia continued to implement a number of large-scale specialist training and retraining programmes, such as Commercial Bank Inspector-Bank Manager, Commercial Bank Curator-Bank Manager and Commercial Bank Receiver-Bank Manager. These programmes are conducted in collaboration with leading Russian institutions of higher education, such as the Russian Government's Academy of the National Economy, the Higher School of Economics and the Russian Government's Financial Academy.

Sixty-three Bank of Russia employees who excelled at these advanced training programmes in 2003 and 2004 continued their training and received a state MBA diploma.

Since 2003, a total of 648 supervisors, of whom 90% are Bank of Russia regional branch managers and experts, have received advanced training or gone through retraining programmes.

In addition, the Bank of Russia continues to implement programmes to improve the social skills and personal efficiency of bank curators and inspectors, who are trained in confidence, partnership, public presentation and partner persuasion skills, development of confidence and ability for co-operation. About 40% of employees have undergone this course of training.

In 2006, the Bank of Russia will continue advanced training or retraining and improve the social skills of its supervisors.

III.2. Upgrading the Legislative and Regulatory Framework of Credit Institutions' Activities in Accordance with International Standards

To implement the Strategy, the Russian Government's Lawmaking Plan until 2008 and Guidelines for the Single State Monetary Policy in 2005, the Bank of Russia continued to make efforts last year to upgrade banking legislation by contributing to the drafting of some federal laws. It particularly emphasised the improvement of applicable legislation to create legal conditions for credit institutions' activities in compliance with international standards.

In line with enacted federal laws, the Bank of Russia implemented measures to improve the regulatory base of the state registration of credit institutions, the licensing of banking operations, banking regulation and supervision and the financial rehabilitation and liquidation of credit institutions.

Insuring household deposits with Russian banks

As regards the measures taken to insure household deposits with Russian banks in 2005, mention should be made of the coming into force of Federal Law of October 20, 2005, No. 132-FZ "On Amending Article 47 of the Federal Law 'On Insurance of Household Deposits with Banks of the Russian Federation'", which allowed banks to appeal against the Bank of Russia's refusal to give them access to the deposit insurance system without simultaneously stripping them of the right to take household funds on deposit. For the purposes of this law, the Bank of Russia in 2005 issued Ordinance of November 22, 2005, No. 1633-U "On Amending Bank of Russia Ordinance of July 16, 2004, No. 1476-U 'On the Procedure for Ordering a Bank by the Bank of Russia to Present a Statement on the Termination of the Right to Handle Deposits'", and Ordinance of December 16, 2005, No. 1640-U "On Amending Bank of Russia Ordinance of July 30, 2004, No. 1483-U 'On the Procedure for Prohibiting a Bank that Refused to Participate in the Deposit Insurance System or Failed to Comply with the Requirements for Participation in the Deposit Insurance System from Taking Household Funds on Deposit and Opening Household Bank Accounts'".

Bank of Russia Instruction of March 24, 2005, No. 123-I "On the Specifics of Co-operation between Bank of Russia Structural Units in Considering a Bank's Repeat Request for the Bank of Russia to Consider its Compliance with the Requirements for Participation in the Deposit Insurance System", established the procedure for informing a Bank of Russia regional branch why a bank had been refused access to the deposit insurance system. It also established the Bank of Russia head office's role in preparing for a selective inspection of a bank that has submitted a repeat request and spelled out the specifics of conducting the final analysis by the Bank of Russia regional branch in question.

Bank of Russia Letter of September 30, 2005, No. 123-T "On the Inspection of Banks to Consider whether they can be Granted Permission to Expand the Range of their Operations by Obtaining Additional Licences", made it possible to consider a request by a credit institution allowed to join the deposit insurance system to grant it permission to take household funds on deposit in foreign currency without conducting a selective inspection if the previous one ended less than a year ago.

Licensing credit institutions' activities

Bank of Russia Regulation of April 19, 2005, No. 268-P "On the Procedure and Criteria for Evaluating the Financial Position of Individual Founders (Members) of a Credit Institution" came into force in 2005. It applies to individuals who intend to acquire shares (stakes) in a credit institution, except individuals registered as private entrepreneurs. The Regulation establishes, within the framework of applicable legislation and for the purpose of evaluating the financial position of individual founders (members) of a credit institution, the documents confirming the sources of the funds paid by individuals as a contribution to the authorised capital of a credit institution. The implementation of the Regulation creates additional safety mechanisms against the adverse effect of criminally obtained capital on credit institutions' activities, which is an objective set in the Strategy.

Bank of Russia Ordinance of February 7, 2005, No. 1548-U "On the Procedure for Opening (Closing) and Operating a Mobile Cash Point of a Bank or Its Branch", established the procedure for opening by a bank or its branch of a new type of internal structural units — a mobile cash point. It is designed to provide banking services in territories with an underdeveloped banking infrastructure, regions that are hard to reach and sparsely populated areas where a permanent bank branch or unit would be loss-making and the provision of banking services to households is inadequate or difficult. The Ordinance lists the cash operations which this point can conduct, sets out the principles of organising it and establishes the requirements for its technical strength and equipment and creates conditions for increasing the banking sector's presence in regions where banking services are rarely provided.

Pursuant to Article 50.37 of the Federal Law "On the Insolvency (Bankruptcy) of Credit Institutions", the Bank of Russia issued Regulation No. 275-P, dated August 11, 2005, "On the Procedure for Issuing a Bank of Russia Licence for Conducting of Banking Operations by a Credit

Institution Whose Bankruptcy Case Has Been Closed in Connection with the Settlement of its Obligations by its Founders (Members) or a Third Party (Third Parties)".

The main requirements for issuing a banking licence are as follows: a credit institution must settle its obligations no later than six months after the revocation of its banking licence; there must be no new claims by creditors or debt on compulsory payments; a credit institution must have an authorised capital matching the Bank of Russia requirement (5 million euros for a bank and 500,000 euros for a non-bank credit institution) and not exceeding its own funds (capital); candidates for the executive positions and the position of a chief accountant and its deputies and members of the board of directors (supervisory board) of a credit institution should meet the established fitness and propriety requirements. The decision to issue a banking licence to a credit institution is taken by the Bank of Russia's Banking Supervision Committee. Should the Bank of Russia decide not to take decision on issuing a banking licence to a credit institution or decide not to issue this licence, the credit institution must be liquidated under the Federal Law "On Banks and Banking Activities".

Bank of Russia Ordinance of October 4, 2005, No. 1624-U amended Bank of Russia Instruction of January 14, 2004, No. 109-I "On the Decision-Making Procedure in Respect to the State Registration of Credit Institutions and the Issue of Banking Licences", for the purpose of further improving the registration process of credit institutions and the licensing of banking operations. Specifically, the Ordinance:

— contains a more detailed list of documents a credit institution or its branch is required to present to a Bank of Russia regional branch in the event of insuring cash to the amount of no less than the minimum permissible cash balance in the cash department and agreeing with the insurance company the requirements for the technical strength of the offices for operations with valuables. The requirements for these offices, established by Bank of Russia regulations, are not presented and, consequently, credit institutions need not submit the technical strength documents to Bank of Russia regional branches;

— contains an exhaustive list of operations a cash point can conduct: cash operations with legal entities and households (accept and pay cash); some banking operations and other transactions with individuals involving foreign exchange, rubles and cheques, including traveller's cheques, whose nominal value is indicated in foreign currency;

— specifies the procedure for issuing to a credit institution new banking licences and the state registration certificate in the form established by the Bank of Russia in case of the expansion of the range of operations, making changes to the founding documents connected with the previous licence's replacement, changing the status of or reorganising credit institutions (taking into account the procedure for terminating "old" licences and certificates).

Bank of Russia Ordinance of November 15, 2005, No. 1632-U made the following amendments to Bank of Russia Regulation of June 4, 2003, No. 230-P "On the Reorganisation of Credit Institutions in the Form of Mergers and Acquisitions", which take into account the proposals made by credit institutions and Bank of Russia regional branches on the basis of their experience in applying Bank of Russia Regulation No. 230-P:

— a credit institution established as a result of a merger or a takeover is granted the right to submit to a Bank of Russia regional branch a letter of commitment to the effect that the documents confirming the ownership (lease, sub-lease or freehold) of a building (office) in which its branch or internal structural unit established on the basis of the reorganised credit institution or its branch will be housed will be presented after the reorganisation is completed. The amendment is brought about by the fact that in some cases reorganised credit institutions are unable to acquire the right of ownership (lease, sub-lease or freehold) of above premises before the reorganisation is completed;

— correspondent accounts of credit institutions or correspondent sub-accounts of branches of credit institutions that have been wound up and the correspondent account of the credit institution that has appeared as a result of the reorganisation of (acquiring) a credit institution or correspondent sub-accounts of its branches opened on the basis of the wound-up credit institutions or their branches may be kept simultaneously for some time. The Bank of Russia takes the corresponding decision upon the receipt of an application from a credit institution and makes this decision known by sending it a letter. The letter establishes the procedure for keeping these correspondent accounts and sets the time period for keeping them (no more than 90 calendar days). The purpose of the amendment is to ensure the fail-safe servicing of customers of the reorganised credit institutions, optimise the redistribution of financial flows and reduce settlement times;

— pursuant to the provisions of the Tax Code of the Russian Federation, the document requires a credit institution to pay a stamp duty to obtain a banking licence. At the same time, it rules out the payment of a licence fee and a fee for opening a branch on the basis of the reorganised credit institution.

Bank of Russia Ordinance of August 11, 2005, No. 1606-U "On the Procedure for Processing Documents that Regulated Credit Institution Operations Before the State Registration of Amendments to the Founding Documents, the State Registration of the Credit Institutions Established as a Result of Reorganisation and Before the Replacement of Banking Licences", established the procedure for invalidating the title documents of credit institutions, on the basis of which they operated before the state registration of the changes made in the founding documents. The Ordinance also established the procedure for the state registration of credit institutions set up through reorganisation and the procedure for replacing banking licences and changing the status of a credit institution. It also specified the requirements for the design of the corresponding stamp and listed its details.

At the same time, the Ordinance stipulated that the issue of new documents to credit institutions is conditional upon the presentation to a Bank of Russia regional branch of the previously issued certificates of state registration in the form established by the Bank of Russia (if a credit institution has such a certificate) and the banking licences on the basis of which credit institutions operated before the aforementioned changes were made. The time period set for the issue of new documents to credit institutions was reduced from five working days to three.

Off-site supervision

The efforts made by the Bank of Russia in 2005 to upgrade the legislative and regulatory framework of off-site supervision aimed to encourage substantive approaches, especially with regard to assessing the nature and level of the risks assumed by a credit institution and the quality of its management and internal control systems.

The Bank of Russia contributed to drafting the following federal laws:

— "On Amending the Federal Law 'On Banks and Banking Activities' and Federal Law 'On the Central Bank of the Russian Federation (Bank of Russia)'" for the purpose of establishing own funds (capital) requirement for the banks at the ruble equivalent of at least 5 million euros, effective as of January 1, 2007;
— "On Amending the Federal Law 'On Banks and Banking Activities' and Federal Law 'On the Insolvency (Bankruptcy) of Credit Institutions'" in respect to the capital adequacy ratio for a credit institution.

The Bank of Russia was instrumental in drafting a law amending the Federal Laws "On the Insolvency (Bankruptcy) of Credit Institutions", "On the Central Bank of the Russian Federation (Bank of Russia)" and the Civil Code of the Russian Federation to legalise the use of internationally accepted subordinated and hybrid instruments (call option subordinated borrowings and hybrid innovation instruments).

It elaborated the concept of a draft federal law to amend the Federal Law "On the Central Bank of the Russian Federation (Bank of Russia)" with the aim of introducing additional control over the risks arising in conducting operations by credit institutions with related parties.

To make the supervision of credit institutions more effective, including supervision on a consolidated basis, the Bank of Russia:

— drafted (in collaboration with the Ministry of Finance) a federal law amending the laws "On Banks and Banking Activities" and "On the Central Bank of the Russian Federation (Bank of Russia)" with the aim of specifying the terms used in these laws and the Bank of Russia's powers to take supervisory decisions with regard to parent credit institutions within banking groups, legitimising the Bank of Russia's powers to supervise bank holding companies and harmonising with IFRS the standards relating to banking groups, bank holding companies and their disclosure of information to users concerned;
— took part in discussing the Finance Ministry draft concept, terms of reference and federal law specifying the requirements for information disclosure by credit institutions, banking groups and bank holding companies and drafted proposals for harmonising these legislative acts with internationally accepted standards and extending the list of federal laws that must be amended for this purpose, namely, the laws "On Joint-Stock Companies" and "On Accounting".

In 2005, the Bank of Russia took part in the discussion of the draft Corporate Law Development Strategy until 2008, prepared by the Economic Development and Trade Ministry. The principal objectives of the draft are to ensure the protection of ownership in the corporate sector, make Russian institutions more competitive, stimulate the stock market's development, provide an adequate legislative basis for business concentration and diversification and upgrade the legal framework of corporate governance. Bank of Russia proposals focused on the following issues:

— creating sources of authorised capital to tackle the problem of capital padding;
— preserving the principle of commensurability of the powers to manage a company, granted to its members (shareholders) with the amount of share (stakes) they own to prevent corporate blackmail;
— preserving for credit institutions the procedure requiring the establishment of a two-tier system of management to ensure that the managerial decisions taken are well balanced and objective and the interests of creditors and depositors are secured;
— preserving the possibility of electing members of executive bodies and independent directors to the board of directors (supervisory board);
— lifting the requirement to elect an audit commission.

The Bank of Russia examined last year Finance Ministry-drafted conceptual proposals for a draft Federal Law "On Consumer Credit", which aimed to create favourable conditions for expanding consumer lending, guarantee the rights of consumers using consumer credit, build a system of safeguards for consumers and provide a legal framework for the development of consumer lending. On some key issues, such as the disclosure of information on consumer loans and measures to protect consumer interests, the Bank of Russia drafted its own proposals designed to make the draft law more amenable to the provisions of Joint Letter of the Federal Antimonopoly Service and the Bank of Russia of May 26, 2005, No. IA/7235/77-T "Recommendations on the Information Disclosure Standards in Consumer Credit".

The efforts made by the Bank of Russia in the field of auditing credit institutions aimed to improve co-operation with the Ministry of Finance and audit organisations to make banking supervision more effective. This co-operation was implemented within the framework of the Finance Ministry's Audit Council and its working groups, set up to upgrade audit laws and work out audit standards on the basis of the International Audit Standards.

The Bank of Russia participated in considering a draft law to amend the Federal Law "On Audit" passed by the lower chamber of parliament in the first of three readings, the Russian Government Resolution "On Measures to Ensure Mandatory Audit", federal audit rules (standards), the model provision "On the External Body of Control over the Quality of Audit Services Provided by Audit Organisations and Individual Auditor Members of the Professional Auditors Association" and methodological recommendations on audit issued by the Audit Commission of the Finance Ministry's Audit Council. In addition, the Bank of Russia submitted proposals to the Finance Ministry for inclusion in the Methodological Recommendations on the Audit of Credit Institutions and Banking (Consolidated) Groups.

To improve the regulation of credit institutions, the Bank of Russia issued regulations and letters establishing the principles of supervision.

The Bank of Russia continued to upgrade bank prudential ratio methodology. It specified inter alia:

— the methods for calculating the assets included in the capital adequacy ratio (N1);
— the methods for calculating the prudential ratios setting a limit on a bank's credit risk.

To tighten control over the risks involved in banks' transactions with related parties, Bank of Russia Letter of January 17, 2005, No. 2-T "On Conducting Bank Transactions with Related Parties and the Assessment of Risks Arising from these Transactions" recommended banks to set relative and (or) absolute limits in their internal documents on the credit risk-carrying transactions with related parties and to establish a procedure for controlling credit risk assessment in transactions with them.

Ordinance of February 18, 2005, No. 1549-U, Ordinance of July 6, 2005, No. 1592-U and Ordinance of July 29, 2005, No. 1599-U "On Amending Bank of Russia Instruction of January 16, 2004, No. 110-I 'On Banks Prudential Ratios"', issued by the Bank of Russia:

— cancelled the general liquidity ratio N5;
— made changes to specify the methods for calculating the assets included in the capital adequacy ratio N1;
— made changes to specify the methods for calculating the prudential ratios limiting a bank's credit risks (N6, N7, N9.1, N10.1 and N12).

To upgrade the country risk assessment methodology, the Bank of Russia issued Ordinance of June 22, 2005, No. 1584-U "On Loan Loss Provisioning and the Size of Loan Loss Provisions for Credit Institutions' Operations with Residents of Off-shore Zones", which came into force on October 1, 2005, it:

— stipulated that the size of provisions depends on the level of country risk, regardless of the level of credit risk involved in operations with residents of off-shore zones;
— required credit institutions to make provisions as soon as their operations with residents of off-shore zones are recorded in accounts and to maintain provisions at an adequate level on a permanent basis;
— systematised the financial instruments for which provisions should be made and brought this list into compliance with the list of financial instruments contained in Bank of Russia Regulation of March 26, 2004, No. 254-P "On the Procedure for Making by Credit Institutions Loan Loss Provisions, Provisions for Loan Debts and Similar Debts" (hereinafter referred to as Regulation No. 254) and Bank of Russia Regulation of July 9, 2003, No. 232-P "On the Procedure for Making by Credit Institutions Provisions against Possible Losses" (hereinafter referred to as Regulation No. 232);
— prohibited credit institutions from writing off uncollectible debt as it is defined in Point 2.3 of Bank of Russia Regulation of March 26, 2004, No. 254-P at the expense of the loan loss provision made for it under Bank of Russia Regulation of June 22, 2005, No. 1584-U.

To upgrade the foreign exchange risk limitation procedure, the Bank of Russia issued Instruction of July 15, 2005, No. 124-I "On Setting Limits on Open Currency Positions, the Methodology for Calculating them and the Specifics of Supervision of their Observance by Credit Institutions"[65]. The principal changes this document makes to defunct Bank of Russia Instruction of May 22, 1996, No. 41 "On Setting Limits on the Open Currency Position and Monitoring their Observance by the Authorised Banks of the Russian Federation", are as follows:

— the requirement to observe the limits set on open currency positions (OCP) must be met by all banks assuming foreign exchange risk, regardless of whether they have or do not have the Bank of Russia licence (permit) to conduct operations with foreign exchange and precious metals, including the operations with the ruble, if the size of ruble positions depends on the change in the exchange rate of foreign currencies and precious metals;
— the OCP calculation includes the provisions made for possible losses on the financial instruments included in the OCP calculation;
— the OCP calculation includes the currency position on capital;
— the Instruction repealed the provision of Bank of Russia Regulation of February 10, 2003, No. 215-P "On the Methodology for Determining Own Funds (Capital) of Credit Institutions", which stipulated that the calculation of OCP limits did not include foreign currency-denominated financial instruments reducing the own funds (capital) indicator, such as investments in non-resident shares (stakes), including the shares (stakes) in subsidiaries, subordinated loans placed and own shares in a bank's authorised capital bought out by the bank and paid for in foreign currency;

[65] Bank of Russia Instruction No. 124-I came into force on February 20, 2006.

- the OCP calculation includes foreign currency-denominated claims and obligations on accrued interest recorded in balance sheet and off-balance-sheet accounts;
- the off-balance-sheet instruments that must be included in the OCP calculation comprise, in addition to irrevocable bank guarantees, irrevocable sureties and letters of credit. The OCP calculation should also include revocable sureties, guarantees and letters of credit, if the corresponding agreements are concluded on terms and conditions similar to those of the agreements on irrevocable guarantees, sureties and letters of credit from the standpoint of legal and economic implications for the guarantor (surety) or warrantor;
- the entire credit institution is subject to control over the OCP observance. Control over the observance of the OCP sub-limits established by a bank for the parent organisation and the branches should be ensured by the bank's management and internal control system;
- the Instruction optimised the OCP reporting procedure. For this purpose, Bank of Russia Ordinance of December 26, 2005, No. 1646-U "On Amending Bank of Russia Ordinance of January 16, 2004, No. 1376-U 'On the List, Forms and Procedure for Compiling and Presenting Reporting Forms by Credit Institutions to the Central Bank of the Russian Federation'"[66], established the procedure for compiling and presenting bank reports in form 0409634 "Statement of Open Currency Positions".

Bank of Russia Letter of February 17, 2005 No. 31-T, "On the Application of Point 2.3 of Bank of Russia Regulation of March 26, 2004, No. 254-P 'On the Procedure for Making by Credit Institutions Loan Loss Provisions, Provisions for Loan Debts and Similar Debts'", explained how credit institutions should establish in their internal documents the procedure for regulating loan loss provisions in connection with the change in the principal amount of the debt.

A number of regulatory documents were drafted last year to improve the Bank of Russia's supervisory requirements.

The Bank of Russia continued to upgrade its supervisory practices to detect cases or signs of fictitious own funds (capital) being created by credit institutions. In 2005, it issued Ordinance of February 6, 2006, No. 1656-U "On Actions to Be Taken in Response to the Detection of Cases or Signs of the Creation of Regulatory Capital or a Part Thereof by Using Improper Assets"[67], which took into account the experience gained by Bank of Russia regional branches in using Bank of Russia Regulation of February 10, 2003, No. 215-P "On the Methodology for Determining Own Funds (Capital) of Credit Institutions", and Bank of Russia Ordinance of February 10, 2003, No. 1246-U "On Actions to Be Taken in Response to the Detection of the Cases or Signs of the Creation of Capital or a Part Thereof by Using Improper Assets".

This Ordinance contains the following new provisions:

- the structural units of the Bank of Russia head office have the power to point out cases or signs of a credit institutions' regulatory capital being created by investors' using improper assets;
- Bank of Russia regional branches have the power to decide for themselves if a bank has used improper assets in regulatory capital creation (up to 10% of the bank's regulatory capital), cover risk and repeal instructions;
- one way to cover risks (apart from reducing a credit institution's authorised capital and replacing assets), arising from the use of improper assets in own funds (capital) creation, is to make loss provisions by banks in accordance with the procedure established by Regulation No. 254-P or Regulation No. 232-P to the amount corresponding to the balance sheet value of the replaced assets and (or) the amount of contingent liabilities assumed by the credit institution.

In 2005, the Bank of Russia drafted and submitted to the Ministry of Justice for registration Regulation of March 20, 2006, No. 283-P "On the Procedure for Making by Credit Institutions Provisions against Possible Losses"[68], Ordinance of March 20, 2006, No. 1671-U "On Amending Bank of Russia Regulation of March 26, 2004, No. 254-P 'On the Procedure for Making by Credit Institutions Loan Loss Provisions, Provisions for Loan Debts and Similar Debts'" and Ordinance of March 20, 2006, No. 1672-U "On Amending Bank of Russia Instruction of January 16, 2004, No. 110-I 'On Banks Prudential Ratios'".

These regulatory documents introduced the following changes:

- they set up the procedure for assessing the risk of losses on assets put in trust by a credit institution;
- they revise the portfolio provisioning methodology to harmonise it with the new version of IAS 39 (2004), excluding for this purpose from the portfolio claims with individual signs of depreciation and requiring banks to make provisions for such claims on an individual basis. The value of the claims (contingent liabilities) that may be included in the portfolio was raised from 0.1% to 0.5% of a credit institution's regulatory capital;
- they specify the procedure for loss provisioning for contingent liabilities of credit nature, taking into account collateral provided for the transactions, similar to the requirements of Section 6 of Regulation No. 254-P, establishing the procedure for making provisions for loans with due account of collateral;

[66] Bank of Russia Ordinance No. 1646-U came into force on February 20, 2006.
[67] Bank of Russia Ordinance No. 1656-U was registered by the Ministry of Justice of the Russian Federation and came into force on March 26, 2006.
[68] The new version of Bank of Russia Regulation of July 9, 2003, No. 232-P "On the Procedure for Making by Credit Institutions Provisions against Possible Losses".

— taking into consideration the new version of IAS 39 (2004), all claims relating to the purchase of securities and other financial assets with an obligation on their subsequent alienation, regardless of who is the counterparty in the transaction, what securities are purchased and whether the contract contains a provision allowing the sale of the securities involved in the transaction, are considered as loans for which provisions should be made in compliance with Regulation No. 254-P;

— the term "guarantee deposit" is re-defined, taking into account the provisions of Article 410 of the Civil Code of the Russian Federation on the complete or partial termination of an obligation by offsetting it against a similar counter-claim.

The principles of corporate governance, adjusted to the institutional and legal specifics of the Russian banking system, the principles of separating the powers between management bodies in a credit institution and the role played by the board of directors (supervisory board) in organising risk management, preventing conflicts of interest, ensuring the observance of the rules of professional conduct and elaborating and implementing the information policy are set out in Bank of Russia Letter of September 13, 2005, No. 119-T "On the Contemporary Principles of Corporate Governance in Credit Institutions".

The operational risk factors, the role played by the board of directors (supervisory board) and executive bodies in organising the management of this risk and the principles of building the operational risk management system are described in Bank of Russia Letter of May 24, 2005, No. 76-T "On Operational Risk Management in Credit Institutions".

The external and internal factors of legal and reputation risks and the principles of establishing the procedure for detecting, assessing and monitoring the level of these risks and minimising them are established in Bank of Russia Letter of June 30, 2005, No. 92-T "On the Management of Legal and Reputation Risks in Credit Institutions and Banking Groups". In addition, the Letter contains recommendations on identifying customers to ensure the observance of the "know-your-customer" principle and recommendations on some personnel-policy issues, including the observance of the "know-your-employee" principle. To improve control over banks interest rates on household deposits, the Bank of Russia sent its regional branches Letter of April 8, 2005, No. 59-T "On Information about Banks Setting Higher Interest Rates on Household Deposits".

Aware of the growing role of the electronic communications and their increased impact on banking, the Bank of Russia issued Letter of January 19, 2005, No. 8-T "On Data Recommended for Placement on Credit Institutions' Web Sites", which recommended credit institutions to put on their web sites information on being accepted to and expelled from the deposit insurance system and the contact details of the Bank of Russia regional branches supervising them.

To further encourage credit institutions to use electronic reporting, the Bank of Russia issued Ordinance of January 24, 2005, No. 1546-U "On the Procedure for Sending Statements by Credit Institutions to the Central Bank of the Russian Federation in the Form of Electronic Authentication Code Messages" and Letter of March 23, 2005, No. 45-T "On the Form of Contract between a Credit Institution and the Bank of Russia on the Transmission and Reception of Electronic Statements".

Inspection

In 2005, the Bank of Russia continued to upgrade the legal regulation of inspection to ensure that the activities of credit institutions are evaluated on the basis of a professional judgement, including the assessment of risk management and internal controls.

To improve the comprehensive system of inspections and bring it into compliance with the requirements of Federal Laws of December 23, 2003, No. 177-FZ "On Insurance of Household Deposits with Banks of the Russian Federation", of December 10, 2003, No. 173-FZ "On Foreign Exchange Regulation and Control", and the Bank of Russia's effective regulations on banking regulation and supervision, the Bank of Russia made some changes in its regulations in 2005 on the procedure for conducting inspections and organising on-site supervision.

Specifically, the Bank of Russia issued Ordinance of January 13, 2005, No. 1543-U "On Amending Bank of Russia Instruction of August 25, 2003, No. 105-I 'On the Procedure for Conducting Inspections of Credit Institutions and their Branches by Authorised Representatives of the Central Bank of the Russian Federation', and Ordinance of January 13, 2005, No. 1544-U "On Amending Bank of Russia Instruction of December 1, 2003, No. 108-I 'On Organising On-site Supervision by the Central Bank of the Russian Federation (Bank of Russia)'".

Bank of Russia inspections of banks to ensure they comply with the requirements of the Federal Deposit Insurance Law represent one condition for the successful establishment and operation of the deposit insurance system. The inspections include those conducted with employees of the Deposit Insurance Agency, a state-run corporation.

In this connection, the Bank of Russia issued Ordinance of January 13, 2005, No. 1542-U "On the Specifics of Conducting Inspections of Banks with Deposit Insurance Agency Employees", and Letter of March 30, 2005, No. 49-T "On Methodological Recommendations for Organising and Conducting Selective Inspections of Banks when Considering their Repeat Requests to the Bank of Russia to Confirm their Compliance with the Requirements for Participation in the Deposit Insurance System".

The inspection and evaluation of internal controls in credit institutions is becoming a major objective of supervision. For this reason, the Bank of Russia sent its regional branches Letter of March 24, 2005, No. 47-T "On Methodological Recommendations for the Inspection and Assessment of Internal Controls in Credit Institutions".

The Bank of Russia continued to take steps last year to improve the quality of inspection materials and raise the standard of preparing these materials. Specifically, to standardise the methods of preparing bank inspection materials, the Bank of Russia issued Letter of February 16, 2005, No. 29-T "On the Registration of Documents Relating to the Organisation and Conduct of Inspections of Credit Institutions and their Branches".

To improve the organisation of on-site supervision and streamline the application of Bank of Russia regulations, the Bank of Russia issued for the staff of Bank of Russia inspection divisions and other authorised representatives of the Bank of Russia Letter of August 11, 2005, No. 110-T clarifying issues arising in organising and conducting inspections of banks by Bank of Russia regional branches.

Financial rehabilitation and liquidation of credit institutions

In 2005, the Bank of Russia continued to improve legislation regulating the financial rehabilitation and liquidation of credit institutions.

At the end of last year, amendments were made to the Criminal Code of the Russian Federation, establishing criminal liability for illegally obstructing the actions of the provisional administration of a credit institution, including a failure or refusal to pass to the provisional administration documents necessary for the fulfilment of its duties or property owned by the credit institution in cases when the functions of the credit institution's manager are assigned to the head of the provisional administration, if these actions (or inaction) caused substantial damage.

Amendments to the Federal Laws "On the Insolvency (Bankruptcy) of Credit Institutions" and "On Banks and Banking Activities" which came into force at the end of 2004 changed the procedure for liquidating credit institutions, as the powers of the receiver (liquidator) of credit institutions with a Bank of Russia licence to take household funds on deposit passed to the corporate liquidator, the Deposit Insurance Agency. In addition, amendments to the bank bankruptcy laws and criminal and administrative legislation considerably increased the responsibility of the founders (members), members of the board of directors (supervisory council) and managers of credit institutions for bringing credit institutions to bankruptcy. The corporate liquidator is also involved in taking legal action against these persons. A legal procedure is currently being established to prosecute persons responsible for bringing banks to bankruptcy, a process that will help change the financial community's perception of the practices used by the managers of bankrupt banks.

In 2005, the Bank of Russia took measures to improve a control mechanism designed to make bank liquidation procedures more effective and open. It also continued to implement the provisions of the Federal Law "On Bank of Russia Payments on Household Deposits with Bankrupt Banks uncovered by the Compulsory Deposit Insurance System" with the aim of increasing the protection of depositors' interests.

Last year, it took part in considering draft laws designed to make the institution of collateral more effective and stronger. Amendments were made to the Civil Code of the Russian Federation to establish the ranking of creditors in the course of liquidating legal entities. Specifically, the provision on the satisfaction of creditors' claims to obligations collateralized by property was brought into line with the provisions of the bankruptcy law.

To facilitate the implementation of the laws on the financial rehabilitation and liquidation of credit institutions, the Bank of Russia issued Instruction of November 11, 2005, No. 126-I "On the Procedure for Regulating the Relations Involved in the Implementation of Measures to Prevent Insolvency (Bankruptcy) of Credit Institutions". It is a part of the package of regulations issued by the Bank of Russia to replace Instruction of July 12, 1999, No. 84-I "On the Procedure for Implementing Measures to Prevent Insolvency (Bankruptcy) of Credit Institutions", and to regulate co-operation between the Bank of Russia regional branches and credit institutions implementing bank insolvency (bankruptcy) prevention measures.

To prevent unjustified delays in implementing insolvency (bankruptcy) prevention measures, the Instruction included a number of additional provisions clarifying for credit institutions the requirements made by the Bank of Russia in the course of implementing such measures. Specifically, the Instruction:

— sets the criteria for the quality and quantity of documents confirming that a credit institution is capable of rehabilitating itself financially;
— specifies the data that must be included in the notification of a credit institution about the decision on its financial rehabilitation or reorganisation;
— establishes the right of a Bank of Russia regional branch to require a credit institution, if necessary, to present individual statements on a daily basis;
— sets up the endorsement procedure for the financial rehabilitation plan, drawn up with the provisional administration, including the cases in which the powers of a credit institution's management are limited or suspended.

Bank of Russia Ordinance of December 30, 2005, No. 1650-U "On the Procedure for Implementing Measures by Bank of Russia Regional Branches to Monitor the Implementation of Insolvency (Bankruptcy) Prevention Measures by Credit Institutions", which came into force simultaneously with Bank of Russia Instruction No. 126-I, regulates internal decision-making procedures in Bank of Russia regional branches in respect to monitoring of insolvency (bankruptcy) prevention measures implemented by credit institutions. The Ordinance set out new principles of control over the implementation of bank insolvency (bankruptcy) prevention measures:

— it requires Bank of Russia regional branches first to make sure if a credit institution can eliminate the grounds for the implementation of insolvency (bank-

ruptcy) prevention measures on its own or with the participation of its shareholders (members), creditors and other persons and only thereafter the Bank of Russia regional branches should decide if they should order the credit institution to implement financial rehabilitation or reorganisation (the previous version of the document required them to issue such an order in any case);
— it established the general principles of passing a professional judgement by Bank of Russia regional branches on the possibility of a financial rehabilitation of a credit institution on the basis of its action plan;
— Bank of Russia regional branches received the powers to decide on their own if it is necessary to conduct unscheduled selective inspections of credit institutions in the course of implementing the financial rehabilitation measures.

Bank of Russia Regulation of November 9, 2005, No. 279-P "On the Provisional Administration of a Credit Institution", which replaced Bank of Russia Regulation of November 26, 2003, No. 241-P set up the procedure for appointing a provisional administration and organising, implementing and terminating its activities. In compliance with Russian legislation, it considerably broadened the functions and powers of the provisional administration in safeguarding the property and assets of a credit institution and established in agreement with the Deposit Insurance Agency (hereinafter referred to as the Agency) a register form of creditors' claims. The Regulation:
— provides for the possibility of arranging co-operation between the Bank of Russia and the Agency by including Agency employees in the provisional administration;
— sets up the procedure for accessing Agency employees to a credit institution's documents without their inclusion in the provisional administration;
— establishes the procedure for publishing information on the activities of the provisional administration and the financial standing of a credit institution;
— sets up the procedure for making claims by creditors and for examining them and the procedure for compiling by the provisional administration of a register of creditors' claims and a register of a bank's obligations to depositors;
— requires the provisional administration to examine a credit institution to search for any signs of insolvency (bankruptcy) or fictitious bankruptcy;
— establishes the procedure to be used by the provisional administration if it is prevented by third persons from fulfilling the functions assigned to it by law or if there is no property, documentation, archive and (or) electronic database of a credit institution at the place of its registration and (or) last known residence;
— sets the procedure for compiling and getting approval for the provisional administration's expense budget and controlling its execution.

Bank of Russia Ordinance of July 14, 2005, No. 1594-U "On the List and Forms of and the Procedure for Compiling and Presenting to the Central Bank of the Russian Federation Statements by Credit Institutions while Being Liquidated", stipulates that these statements should contain information on bankruptcy assets, property stocktaking, evaluation and sale results, the returns from sale, their expenditure on the credit institution's operations and the settlement of creditors' claims. The statements are used for control of the agency liquidating the credit institution in the interests of creditors (depositors).

III.3. Bank of Russia Assessment of Banks' Compliance with Deposit Insurance System Requirements

While implementing the Federal Deposit Insurance Law (hereinafter referred to as the Federal Law), the Bank of Russia completed in 2005 its assessment of how banks licensed to take household funds on deposit at the time this Law came into force complied with the requirements for participation in the deposit insurance system.

The work of the Bank of Russia was aimed at evaluation of banks' performance and their ability to safeguard the interests of creditors and depositors, as well as to minimise the risks to which the banks are exposed. Information received by the Bank of Russia during off-site supervision and selective inspections allowed it to improve banking supervision in terms of evaluating the financial soundness of individual banks and the stability of the banking system as a whole, as well as determining banking sector development trends and areas that have yet to be regulated legislatively.

Requests for admission to the deposit insurance system were filed with the Bank of Russia by the deadline set under the Federal Law by 1,150 banks[69] that had a licence to take household funds on deposit (1,183 banks had this licence as of June 27, 2004).

As of January 1, 2005, the Bank of Russia granted the requests of 415 banks[70]. In addition, six banks that had requested permission to expand the range of their activities were granted licences to take household funds on deposit. Seven banks were subsequently reorganised. By January 1, 2005, the requests of 67 banks had been rejected.

Following the procedure established by the Federal Law, the Bank of Russia considered in 2005 first-time and repeat requests lodged by banks and appeals to the Bank of Russia's Banking Supervision Committee and Bank of Russia Chairman against decisions to reject repeat requests.

As of March 27, 2005, 817 banks had their first-time requests granted and were admitted to the deposit insurance system (two wound up their operations due to reorganisation) and two banks were granted admission after their repeat requests had been considered. In addition, seven banks were granted a licence to take household funds on deposit.

Having considered the repeat requests of 265 banks, the Bank of Russia granted the requests of 92 banks and turned down the repeat requests of 165 banks; four banks recalled their repeat requests and four banks had their banking licence revoked pending a decision from the Bank of Russia's Banking Supervision Committee. In addition, 11 banks were granted a licence to expand the range of their activities and take household funds on deposit. As a result, another 103 banks[71] were admitted to the deposit insurance system.

The Bank of Russia's Banking Supervision Committee considered the appeals filed by 142 banks against the rejection of their repeat requests, of which the appeals of five banks were granted and the appeals of 137 banks were rejected. The Bank of Russia Chairman considered the appeals of 131 banks against the rejection of their repeat requests and granted the appeals of seven banks, turned down the appeals of 123 banks and one bank had its banking licence revoked while its appeal was under consideration.

When considering requests and appeals, the Bank of Russia particularly focused on verifying banks' accounting and reporting reliability, its compliance with the required ratios, the transparency of its ownership structure, quality of management and internal controls, own funds (capital), how it observed provisioning requirements and ensuring there were no grounds for taking corrective actions. The Bank of Russia made certain that the decisions on banks compliance with the requirements for admission to the deposit insurance system were taken on a collective basis.

As of January 1, 2006, 931 banks[72] holding 2,738 billion rubles in household deposits (94.9% of total household deposits with Russian banks) and 9,255 billion rubles in assets (94.9% of aggregate banking sector assets) were registered with the deposit insurance system. The Bank of Russia turned down 191 requests made by banks that had the licence to take household funds on deposit at the time when the Federal Law came into affect, of which 24 banks had their banking licences revoked as of January 1, 2006.

The Bank of Russia constantly monitors how banks registered with the deposit insurance system are complying with its requirements. If a bank fails to comply with these requirements for three consecutive months, the Bank of Russia must, pursuant to Article 48 of the Feder-

[69] Including banks that recalled their requests while they were considered, banks that had their banking licences revoked while their requests were considered and banks that wound up their operations due to reorganization before any decision was made on their requests.

[70] As of January 1, 2005, the Deposit Insurance Agency had 381 banks on the register of the banks participating in the deposit insurance system.

[71] Five of them wound up their operations due to reorganization.

[72] Including 20 banks which were granted licences to expand the range of their activities and take household funds on deposit and excluding banks that were admitted to the deposit insurance system but subsequently wound up their activities due to reorganization.

al Law, prohibit this bank from taking household funds on deposit and opening individual bank accounts.

The deposit insurance system has increased public trust in the banking system and has had a positive effect on the stability of the financial markets and the economy as a whole. The banks that have passed through the selection procedure have improved the quality of their own funds (capital) and assets significantly, upgraded their internal corporate governance systems and adjusted their internal controls. As a result, banks have become more efficient and competitive, and the banking sector has become more transparent. Banks that broke the law and Bank of Russia rules and regulations have had their licences revoked. The methodology developed by the Bank of Russia and the experience it gained while considering banks requests and taking decisions on them are now used by the Bank of Russia in its day-to-day activities and help it improve banking supervision.

Insurance compensation was paid out on household deposits when a bank registered with the deposit insurance system had its banking licence revoked in 2005. This case showed that the Bank of Russia had not only established an efficient procedure for making the insurance fund, but had also resolved technical difficulties in settling accounts with depositors. It also served as a reminder that the deposit insurance system is designed to protect depositors rather than guarantee immunity to bank owners and managers.

III.4. Registration and Expansion of Credit Institutions Activities

The decline in the total number of registered credit institutions continued in 2005 and last year the total number of registered credit institutions decreased from 1,516 to 1,409, or by 7% as against 9% in 2004, when their total number fell from 1,666 to 1,516. The number of operating credit institutions with a banking licence declined from 1,299 in 2004 to 1,253 in 2005, of which 48 were non-bank credit institutions *(see Chart 3.1 and Chart 3.2).*

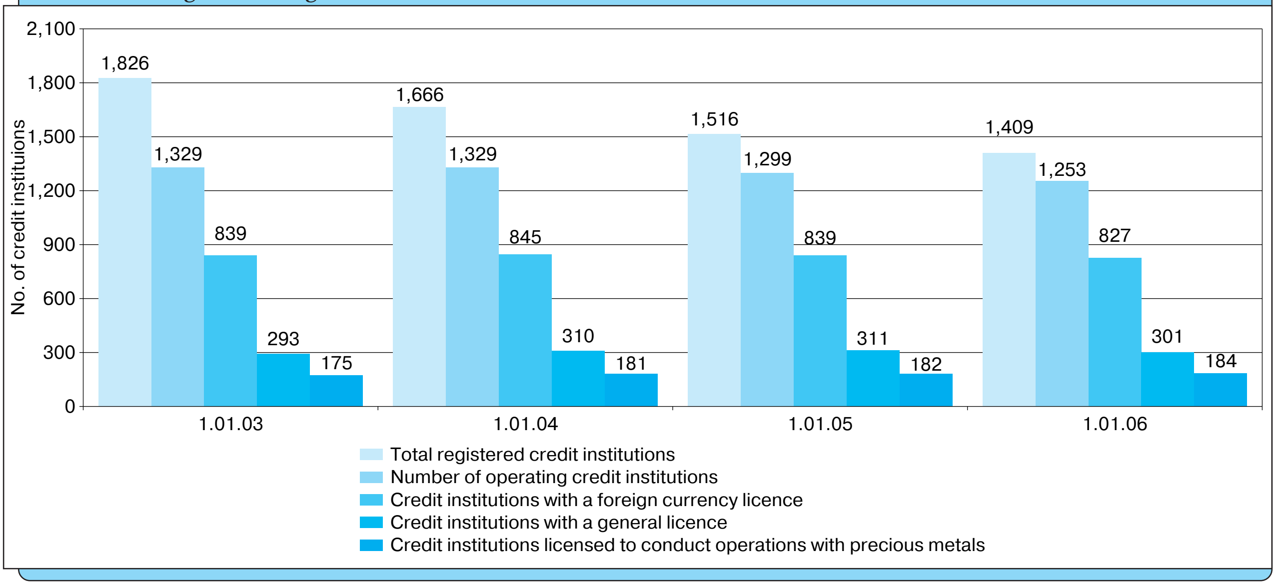
Nine new credit institutions were registered in the year under review: six were banks and three non-bank credit institutions. This compares with three credit institutions registered in 2004 (two banks and one non-bank credit institution) and 16 registered in 2003 (14 banks and two non-bank credit institutions).

The reorganisation of credit institutions continued in the year under review: 14 credit institutions merged with other credit institutions (as against three in 2004), four credit institutions changed their organisational and legal status from limited liability companies to joint-stock companies (as against five in 2004 and nine in 2003), one credit institution turned from an additional liability company into a joint-stock company and one credit institution was transformed from a state-run enterprise into a joint-stock company.

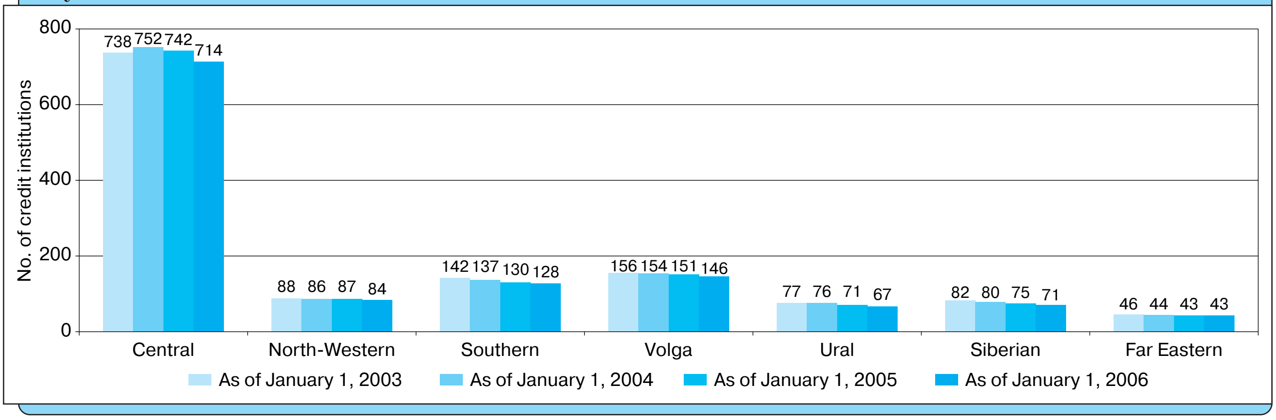
In 2005, as in 2004, one non-bank credit institution became a bank (no bank became a non-bank credit institution in 2005 or 2004).

Fifty-nine credit institutions, or 4.7% of the total, expanded the range of their operations in 2005 by obtain-

Dynamics of the number of registered operating credit institutions and banking licences granted to them *CHART 3.1*



Dynamics of the number of credit institutions by federal district *CHART 3.2*



ing additional banking licences (54 credit institutions, or 4.16% of the total in 2004). These credit institutions received 11 general licences, 11 licences to conduct operations with foreign exchange and 10 licences to take on deposit and place precious metals.

Fourteen banks were granted permission to take household funds on deposit for the first time in 2005.

The principal objective of the *Russian Banking Sector Development Strategy until 2008* is to make the banking system more stable and efficient. While seeking to do this, the Bank of Russia rejected the requests of a number of credit institutions that wanted to expand the range of operations by obtaining additional licences in 2005:

— four credit institutions had their first-time requests for a licence to take household funds on deposit rejected because they failed to comply with the requirements set by the Federal Law “On Insurance of Household Deposits with Banks of the Russian Federation”;

— 13 credit institutions had their requests for other types of licences turned down because they committed the following violations of laws and Bank of Russia rules and regulations: their internal controls were inadequate to the scale of their banking operations and the risks they assumed, their financial soundness did not satisfy Bank of Russia requirements and the Bank of Russia had no information about the persons or groups of persons who directly or indirectly (through third persons) exerted substantial influence on the decisions taken by bank management, etc.

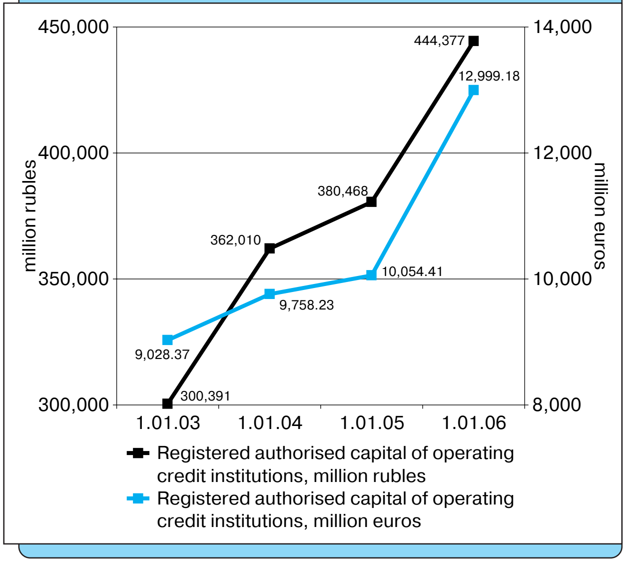
In comparison, 17 credit institutions were refused additional licences in 2004.

The measures taken by shareholders and members of credit institutions in 2005 allowed operating credit institutions to increase their aggregate authorised capital by 63.9 billion rubles — or 16.8% — from 380.5 billion rubles to 444.4 billion rubles. In 2004, the aggregate authorised capital of operating credit institutions increased by 18.5 billion rubles, or 5.1% *(see Chart 3.3).*

The number of credit institutions with a registered authorised capital of less than 60 million rubles continued to decrease and their share continued to contract in the year under review, whereas the number of credit institutions with a registered authorised capital of more than 60 million rubles continued to increase.

As of January 1, 2006, there were 243 operating credit institutions with an authorised capital of more than 300 million rubles, or 19.4% of the total number of operating credit institutions (nine more than on January 1, 2005, and 35 credit institutions more than on January 1, 2004, an increase by 17%). The number of credit institutions with an authorised capital of between 150 million rubles and 300 million rubles rose to 204, or 16.3% of the total (it increased by 13 as compared with January 1, 2005, and by 38, or by 23%, as compared with January 1, 2004). The number of credit institutions with an authorised capital of between 60 million rubles and 150 million rubles reached 227, or 18.1% of the total, increasing by 16 as

Dynamics of registered authorised capital of operating credit institutions CHART 3.3



compared with January 1, 2005, and by 22, or by 11%, as compared with January 1, 2004. *(See Chart 3.4).*

The number of operating credit institutions with a registered authorised capital of between 10 million rubles and 30 million rubles and from 30 million rubles to 60 million rubles stood at 205 and 212 respectively as of January 1, 2006, as against 232 and 225 respectively as of January 1, 2005 (267 and 240 as of January 1, 2004). These credit institutions accounted for 16.4% and 16.9% of the total respectively.

The number of credit institutions with an authorised capital of less than 10 million rubles continued to decline and their share continued to contract (from 15.9% as of January 1, 2005, to 12.9% as of January 1, 2006).

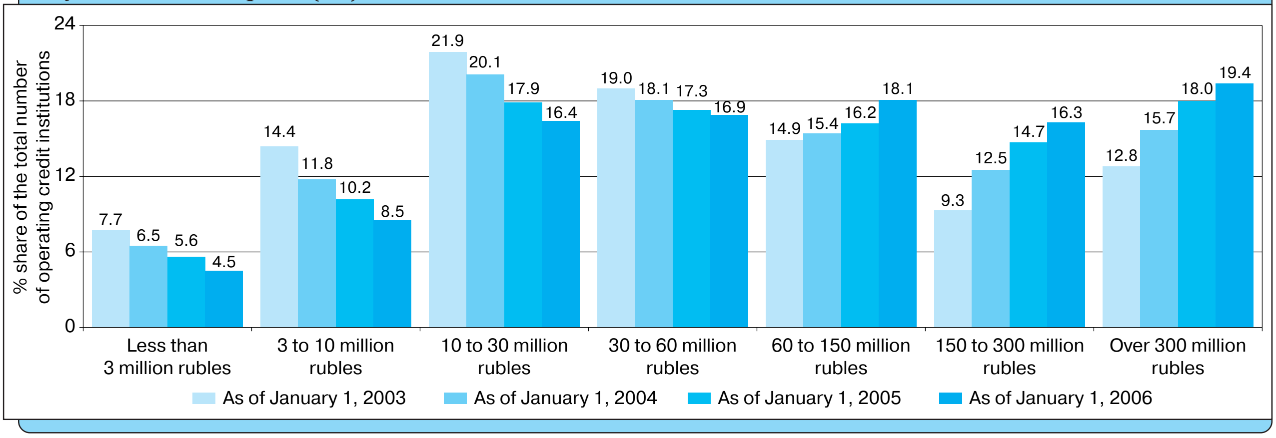
The year under review saw an expansion of foreign capital in the Russian banking system. Non-resident shareholdings in the authorised capital of operating credit institutions increased from 23,553 million rubles in 2004 to 49,554.5 million rubles in 2005, or by 110% (2004 growth stood at 24.6%). The non-resident share in the aggregate authorised capital of the Russian banking sector expanded by 5 percentage points, from 6.2% to 11.2% (in 2004, it increased by one percentage point). The number of operating credit institutions with foreign shareholdings rose from 131 to 136 (in 2004, from 128 to 131), whereas the number of credit institutions with non-resident shareholdings exceeding 50% increased from 42 to 52 (in 2004, from 41 to 42) *(see Chart 3.5).*

Credit institutions with foreign investment are located in 30 constituent members of the Russian Federation. Eighty-eight of them, or 64.7% of the total, are based in Moscow and the Moscow Region and eight in St Petersburg.

Last year, the value of securities issued by credit institutions increased significantly. Most of this growth was due to bond issues: the value of the registered bond issues increased by 3.7 times over the year under review, to 85.7 billion rubles as against 23.3 billion rubles in 2004.

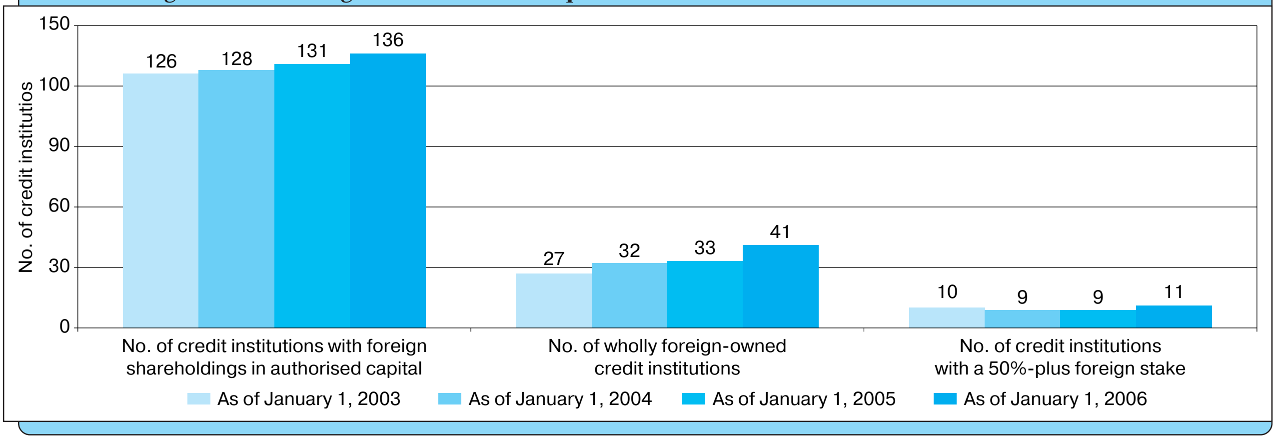
Dynamics of the number of operating credit institutions by authorised capital (%)

CHART 3.4



Dynamics of the number of operating credit institutions with foreign shareholdings in authorised capital

CHART 3.5



The value of the registered share issues increased from 50.3 billion rubles to 85.2 billion rubles, or by 69.4%.

As the authorised capital of credit institutions increased, 246 share issues with a total value of 79.8 billion rubles were registered in 2005, an increase of 36.6 billion rubles, or 84.7%, on 2004.

Authorised capital grew mostly as a result of additional share issues: 236 additional share issues with a total value of 78.4 billion rubles were registered in the year under review as against 234 share issues with a total value of 39.2 billion rubles in 2004. Of these, 11 additional share issues with a total value of 15.1 billion rubles were registered in connection with bank mergers (three share issues with a total value of 200 million rubles were registered for this purpose in 2004).

The largest additional share issue registered in connection with a merger amounted to 12.8 billion rubles and was placed by open-end joint-stock Uralsib company taking over four banks.

Preferred stock accounted for a small part of the shares issued by credit institutions: in 2005, they registered three issues of preferred shares with a total value of 700 million rubles, as compared with four issues with a total value of 100 million rubles registered in 2004.

Stock issued to increase its nominal value accounted for 1.8% of the stock issued to expand authorised capital: 10 share issues with a total value of 1.4 billion rubles were registered for this purpose in 2005 as against 12 share issues with a total value of 4.2 billion rubles in 2004.

Seven share issues with a total value of 2.8 billion rubles were registered in connection with credit institutions reorganisations.

Twenty-eight credit institutions registered 33 bond issues with a total value of 85.7 billion rubles in 2005, of which 26 credit institutions placed 84.4 billion rubles of bonds on the MICEX stock exchange.

Commercial banks based in the Moscow Region remained leaders on the bond market: they made 25 bond issues with a total value of 78.5 billion rubles, or 91.6% of the total value of bonds issued last year. Vneshtorgbank made one of the biggest bond issues with a value of 30 billion rubles. Most credit institutions use a standard bond issue tactic: the market is dominated by medium-term coupon bonds with a maturity period of at least three years, a nominal value of 1,000 rubles and the possibility of a subsequent buy-out at the request of or in agreement with bondholders by making irrevocable public offers.

III.5. Off-site Supervision

In 2005, the Bank of Russia continued to upgrade banking regulation and supervision, taking into account international best practice, including the practice summarised in the documents of the Basel Committee on Banking Supervision. It carried out a series of measures to increase banking sector stability, protect the interests of creditors and depositors, as well as to ensure credit institutions compliance with federal laws and Bank of Russia rules and regulations issued in pursuance of these laws.

The Bank of Russia attached paramount importance to the inclusion of banks in the deposit insurance system, ensuring that only financially sound banks had access to it.

Integrating the results of the Bank of Russia effort to examine banks' compliance with the requirements of banks admission to the deposit insurance system and information received about the credit institutions while considering their applications are of great importance for the risk-based supervision of credit institutions and control over the process to eliminate shortcomings discovered in their work. The banks in the deposit insurance system are monitored on a monthly basis to check how they are complying with the system's requirements. While selecting credit institutions to the deposit insurance system, the Bank of Russia also considered capital quality. It continued to search for evidences that own funds (capital) ware being formed by using improper assets. At the same time, it attached great importance to analysing the quality of assets, their proper classification by risk profile and the amount of loss reserves. At the request of the Bank of Russia 19 credit institutions made corrections to their own funds (capital) in 2005 to the total amount of 6.03 billion rubles.

In 2005, the Bank of Russia continued to lay particular emphasis on informal measures in fighting violations of laws and regulations. After analysing credit institutions' statements, within the scope of informal measures it notified in writing the management and/or boards of directors (supervisory boards) of 1,133 banks about shortcomings detected in their work in 2005 (1,175 banks received such notices in 2004) and held meetings with the top managers of 392 banks.

In 2005, the Bank of Russia within the scope of formal measures prohibited 202 banks from taking household funds on deposit (34 banks in 2004)[73] and 51 banks were prohibited from opening branches (50 banks in 2004). The Bank of Russia also applied sanctions such as fines for a failure to comply with reserve requirements, violations of federal laws and Bank of Russia rules and regulations issued in pursuance of these laws and nonreporting, underreporting and misreporting. A total of 836 banks were censured for various instances of malpractice in 2005 as against 764 banks in 2004. Forty banks had their banking licences revoked in 2005 (33 banks in 2004).

In 2005, the Bank of Russia analysed for the first time credit institutions' (unconsolidated) financial statements compiled according to IFRS for the first nine months of 2004. The analysis was made by comparing credit institutions' performance indicators and data according to their IFRS statements and statements compiled according to Russian accounting rules. The Bank of Russia examined factors that affected a change in individual balance sheet items, own funds (capital) sources and financial results.

As consumer lending expanded and problems with unfair advertising practices in this area arose, the Bank of Russia inspected banks and their branches to make sure that they followed Recommendations of May 26, 2005, No. IA/7235/77-T "On Information Disclosure Standards in Consumer Lending", issued by the Federal Antimonopoly Service and the Bank of Russia.

To prevent as early as possible banking risks that may jeopardise banking sector financial stability, the Bank of Russia monitored banking sector liquidity, the risks involved in consumer lending, and market risk and stress tested the banking sector *(see Annex IV.3 and Annex IV.4).* Provided with monitoring results, Bank of Russia regional branches took supervisory measures against the banks in which unfavourable trends were detected.

In 2005, the Bank of Russia monitored and analysed interest rates on household deposits by maturity and currency. In case a credit institution paid interest on deposits that exceeded the region's average by more than one-fifth the Bank of Russia analysed justification of its interest policy. Bank of Russia regional branches held meetings with some credit institutions and sent letters to others suggesting them to consider expediency of changing their interest rate policy. Some banks cut interest rates on household deposits as a result. Judging by data compiled by Bank of Russia regional branches, higher-than-average interest rates did not signify problems in the banks that set them.

[73] The number of credit institutions prohibited from conducting individual operations, including taking household funds on deposit, increased due to the restrictive provisions of Article 47 of Federal Law of December 23, 2003, No. 177-FZ "On Insurance of Household Deposits with Banks of the Russian Federation".

To provide organisational and methodological support to its regional branches, the Bank of Russia:

— drafted recommendations on the practical application of enterprise monitoring results by Bank of Russia supervisors;

— took steps to bring the "Recommendations for the Analysis of Credit Institutions' Activities and the Development of Banking Services in a Region" into conformity with the changes in the accounting rules and the procedure for compiling and presenting some forms of statements by credit institutions to the Bank of Russia.

In 2005, the Bank of Russia completed the first-stage survey of credit institutions in the field of internet banking. The survey revealed the specifics of this way of providing banking services and the sources (factors) of typical banking risks, as well as assessing their possible effect on the financial soundness of credit institutions. The findings will be used by the Bank of Russia in drafting recommendations on internet banking. In addition, the Bank of Russia studied banks' web sites to make sure that credit institutions were not being used for illegal purposes or in any other way that may harm their business reputation.

In connection with the Bank of Russia participation in the IMF Coordinated Compilation Exercise for Financial Soundness Indicators (FSIs), the Bank of Russia compiled and provided to the IMF the draft FSI metadata *(see Annex IV.2).*

The Bank of Russia pays particular attention to the transparency of individual credit institutions and the banking sector as a whole. In 2005, it published its annual *Banking Supervision Report* and continued to publish the monthly online version of the *Russian Banking Sector Review.*

The share of credit institutions that agreed to disclose information about their activities on the Bank of Russia web site in line with Bank of Russia Ordinance, of March 27, 1998, No. 192-U "On Additional Measures to Protect the Interests of Bank Depositors", expanded from 57.6% in 2004 to 62.2% in 2005.

To provide effective information support for the structural units of its head office and regional branches and optimise technological co-operation inside the Bank of Russia system and with credit institutions, the Bank of Russia continued to establish a single information support system for banking sector regulation and development in 2005.

As part of this project, the Bank of Russia completed a study of business information flows between Bank of Russia supervisory divisions and determined the priorities of a single information system (creating a single information space, reducing to a minimum overlapping information flows, cutting the number of reporting forms, reducing to a minimum the paper document turnover and standardising and automating the exchange of information), which form the basis of this system development concept.

III.6. On-site Inspection of Credit Institutions

In line with the Summary Plan of Comprehensive and Selective Inspections of Credit Institutions (their Branches), Bank of Russia authorised representatives conducted 1,573 inspections in 2005, of which 703 inspections were made in credit institutions, 676 in the branches of credit institutions and 194 in the branches of Sberbank of Russia.

Interregional inspections were performed in 234 credit institutions and their branches, of which 45 inspections were conducted in credit institutions, 110 in the branches of credit institutions and 79 in Sberbank branches.

While conducting scheduled inspections, Bank of Russia authorised representatives paid particular attention to how credit institutions complied with the requirements of the Federal Law "On Countering the Legalisation (Laundering) of Earnings Obtained in an Illegal Way and the Financing of Terrorism". They also focused on the level of risk taken by credit institutions, risk management systems, internal control efficiency in credit institutions, cash discipline, reporting and accounting credibility, capital adequacy, compliance with the authorised capital rules and regulations, as well as how credit institutions were eliminating violations detected by previous inspections.

One of the most important areas of Bank of Russia work in 2005, connected with banking sector stability and the protection of the interests of creditors and depositors, was the organisation and holding inspections of credit institutions (their branches) in compliance with the requirements of the Federal Law "On Insurance of Household Deposits with Banks of the Russian Federation".

In compliance with the requirements of Article 45 of this law, the Bank of Russia conducted 264 selective inspections at the repeat requests of credit institutions.

In 2005, the Bank of Russia closely co-operated with the Deposit Insurance Agency in organising and conducting inspections of the banks in the deposit insurance system. Bank of Russia authorised representatives with Agency employees performed 48 inspections to verify banks' compliance with the requirements of the Federal Law "On Insurance of Household Deposits with Banks of the Russian Federation".

The implementation of the deposit insurance programme allowed the Bank of Russia to take a closer look at the structure of the banking system and the relationship between its regional branches and inspectors with banks, identify the most urgent problems and compile the necessary statistical data. An analysis of all the findings will help the Bank of Russia develop new approaches and elaborate inspection techniques. In 2005, the Bank of Russia also held 648 unscheduled inspections of credit institutions and their branches, including 14 comprehensive ones. In most cases (608) inspections were carried out because a bank was seeking to join the deposit insurance system, wanted to increase its authorised capital by more than 20% of the registered amount, had requested permission to expand the range of activities or was carrying out insolvency (bankruptcy) prevention measures under Article 4 of the Federal Law "On the Insolvency (Bankruptcy) of Credit Institutions".

Unscheduled inspections were also conducted to verify credit institutions' compliance with the Federal Law "On Countering the Legalisation (Laundering) of Earnings Obtained in an Illegal Way and the Financing of Terrorism", Bank of Russia rules and regulations on cash operations, cash movement through customer accounts, cash management and settlement and payment discipline in credit institutions.

Credit institutions found to have violated federal laws during inspections conducted by the Bank of Russia and its regional branches were penalised and even had their banking licences revoked.

To make inspections more effective, the Bank of Russia constantly monitored the quality of inspections of credit institutions (their branches) held by its regional branches. After analysing inspection materials, it sent reports and recommendations to regional branches. In the year under review, the Bank of Russia sent 254 reports of this kind to its 59 regional branches.

In 2005, the Bank of Russia continued to organise and co-ordinate supervision and inspection in the Chechen Republic. It collected and analysed the statements by credit institutions divisions. In the year under review, the Bank of Russia examined documents relating to the opening of seven additional offices and cash offices of the banks operating in the republic and held on-site inspections.

III.7. Financial Rehabilitation and Liquidation of Credit Institutions

Performing the functions of the banking supervisory authority, the Bank of Russia actively participates in the financial rehabilitation of the banking system. Its major objective in this field is to prevent bank bankruptcies. The number of credit institutions meeting the criteria for the implementation of insolvency (bankruptcy) prevention measures declined from 16 as of January 1, 2005, to nine as of January 1, 2006, which illustrates the effectiveness of Bank of Russia measures in this field.

In 2005, credit institutions increasingly took action on their own to eliminate problems that could lead to the enforcement of the bankruptcy prevention measures against them without waiting for the Bank of Russia to order them to do so. The share of the total number of credit institutions liable to actions required by Article 4 of the Federal Law “On the Insolvency (Bankruptcy) of Credit Institutions” expanded from 41% in 2004 to 45% in 2005.

In 2005, the Bank of Russia ordered 23 credit institutions to rehabilitate themselves financially; 17 credit institutions were required to match their authorised capital with own funds (capital).

In the year under review, the Bank of Russia monitored 13 credit institutions to ensure that they carried out their financial rehabilitation plans; 10 credit institutions recovered.

To protect the interests of creditors (depositors) of problem credit institutions, the Bank of Russia appointed provisional administrations to run them.

In 2005, the Bank of Russia oversaw the activities of 49 provisional administrations of credit institutions. Over that period, it terminated the activities of 41 provisional administrations, 14 were dissolved as a result of an arbitration court’s decision to liquidate the credit institutions and appoint their liquidators and 27 provisional administrations were disbanded as a result of an arbitration court’s decision to declare the credit institutions insolvent (bankrupt) and put them into the receivership. Representatives of the Deposit Insurance Agency worked in 16 provisional administrations of credit institutions last year.

In 2005, the Bank of Russia, guided by Article 74 of the Federal Law “On the Central Bank of the Russian Federation (Bank of Russia)” and Articles 20 and 23 of the Federal Law “On Banks and Banking Activities”, issued orders to revoke banking licences from 40 credit institutions, five credit institutions had their licences revoked. Fourteen credit institutions had their licences revoked for repeated violations within a year of the requirements set in Articles 6 and 7 (except paragraph 3 of Article 7) of the Federal Law “On Countering the Legalisation (Laundering) of Earnings Obtained in an Illegal Way and the Financing of Terrorism” (two credit institutions were stripped of their licences for this reason in 2004) and 10 credit institutions had their licences revoked for failing to fulfil creditors’ claims on pecuniary obligations and (or) effect compulsory payments (19 credit institutions in 2004).

The total value of creditors’ claims on 104 credit institutions liquidated and struck off the Unified State Register of Legal Entities in 2005 stood at 86,199.9 million rubles, of which claims to the amount of 16,105.7 million rubles, or 18.7% of the total, were met. Of this amount, 10,484.5 million rubles, or 94.7%, were paid to creditors of first priority.

As of January 1, 2006, 1,305 credit institutions had their licences revoked and were liquidated (see Chart 3.6). The total value of creditors’ claims on these credit institutions stood at 335,552.6 million rubles, of which claims to the amount of 31,381.3 million rubles, or 9.4% of the total claims, were met. 16,426.0 million rubles, or 77.1%, were paid to creditors of first priority.

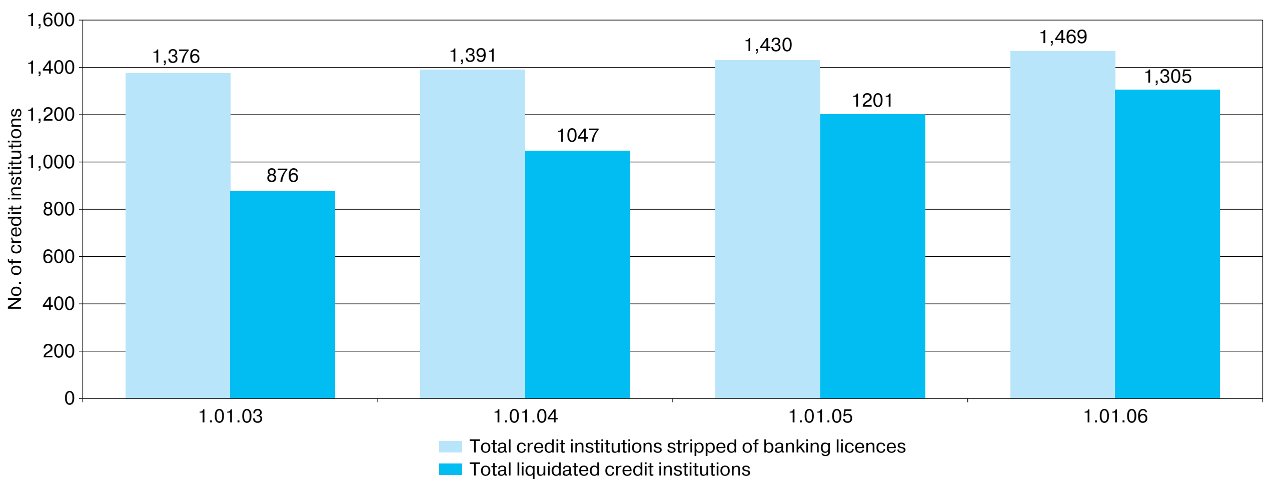
Bankruptcy proceedings have been completed in 46 out of 51 credit institutions pronounced absent debtors by arbitration courts and in which the liquidation procedures were conducted by Bank of Russia employees (these include 13 credit institutions against which bankruptcy proceedings were completed in 2005). In most of these credit institutions the liquidation procedures were completed within a year.

A total of 154 credit institutions were not liquidated even though decisions to liquidate 146 of them had been taken. Most of the liquidated credit institutions (111) were declared bankrupt by arbitration courts and bankruptcy proceedings were initiated against them (these include 35 credit institutions declared bankrupt and subjected to bankruptcy proceedings in 2005); arbitration courts appointed liquidators to 26 credit institutions (12 in 2005); in three credit institutions liquidation proceedings are under way following a decision by their members (founders) and creditors to go bankrupt and wind up voluntarily (according to the rules and standards that were in effect at that time); six credit institutions are being liquidated by the decision of their members (these include four credit institutions that decided to close down in 2005).

As of January 1, 2006, the Deposit Insurance Agency, which is the receiver (liquidator) of credit institutions that took household funds on deposit and in absent debtor credit institutions, was appointed by the arbitration court as the receiver (liquidator) of 46 credit institutions (in 45 of them in 2005), of which 38 credit institutions have been declared bankrupt and subjected to bankruptcy proceedings and eight are being forcibly liquidated.

The Federal Law “On the Insolvency (Bankruptcy) of Credit Institutions” stipulates that the receivers accredit-

Number of credit institutions (on accrual basis) stripped of banking licences by Bank of Russia and number of liquidated credit institutions *CHART 3.6*



ed with the Bank of Russia should be appointed as the receivers of bankrupt credit institutions that had no Bank of Russia licence to take household funds on deposit.

Twenty-seven receivers were accredited with the Bank of Russia in 2005.

In addition, the Bank of Russia extended the terms of the certificates of the receivers (liquidators) of credit institutions against which the bankruptcy proceedings were initiated before Federal Law of August 20, 2004, No. 121-FZ "On Amending the Federal Law 'On the Insolvency (Bankruptcy) of Credit Institutions' and Invalidating Some Laws and Provisions of Some Laws of the Russian Federation" came into force. The terms of 117 receivers' (liquidators') certificates were extended in 2005.

The Bank of Russia conducted 14 inspections of the receivers (liquidators) of credit institutions in 2005. After these inspections receivers (liquidators) were ordered to eliminate the shortcomings discovered in their work. Information about inspection results was sent to arbitration courts, bank creditors committees, the Federal Registration Service and self-regulating receivers organisations of which they are members.

Pursuant to the Federal Law "On Bank of Russia Payments on Household Deposits with Bankrupt Banks Uncovered by the Deposit Insurance System", the Bank of Russia Board of Directors took the decision to pay compensation to depositors of 18 bankrupt banks in 2005. There were 25,773 depositors and the Bank of Russia paid a total of 511.1 million rubles to them.

As of January 1, 2006, the Bank of Russia paid 484.3 million rubles to 21,950 depositors of these bankrupt banks.

III.8. Central Catalogue of Credit Histories

Federal Law of December 30, 2004, No. 218-FZ "On Credit Histories" (hereinafter referred to as Federal Law 218-FZ), assigned to the Bank of Russia the function of keeping the Central Catalogue of Credit Histories (CCCH). Pursuant to this law, the Bank of Russia established in 2005 the CCCH for the purpose of collecting, storing and providing to credit history makers and users information on the credit bureau, in which credit histories are kept, and storing the databases of liquidated (reorganised or struck off the state register) credit bureaux.

To specify the powers of the Bank of Russia in respect to keeping the CCCH and ensuring additional protection of information, the Russian Parliament passed Federal Law of July 21, 2005, No. 110-FZ "On Amending the Federal Law 'On Credit Histories'", which was drafted taking into account Bank of Russia proposals. This law:

— provided the legislative framework for co-operation between the CCCH and credit history persons and users, maintained electronically through the CCCH automated system, and for the powers of the Bank of Russia to establish the formats of requests made by credit history makers and users to the CCCH and the formats of CCCH replies;

— introduced in Federal Law No. 218-FZ the code (additional code) of a credit history person;

— provided for the establishment by the Bank of Russia of the procedure for creating, replacing and cancelling the credit history persons' codes and additional codes;

— provided for the use of different ways of making inquiries by credit history persons and users to the CCCH without using the credit history person's code.

In 2005, the Bank of Russia also took part in drafting proposals and formulating its position on some laws and amendments to them for the purpose of amending Federal Law No. 218-FZ, particularly in respect to the duty of a credit history source to request permission from the credit history person to pass information from the credit history to the credit bureau.

Pursuant to Federal Law No. 218-FZ, the Bank of Russia created the necessary regulatory framework for the functioning of the CCCH.

Bank of Russia Ordinance of August 31, 2005, No. 1610-U "On the Procedure for Requesting and Receiving Information from the Central Catalogue of Credit Histories by Credit History Persons and Users through the Bank of Russia's Web Site", established the procedure for requesting information by credit history persons and users directly from the CCCH about the credit bureaux where the credit histories are kept and receiving this information from the CCCH and the procedure for changing and cancelling a credit history person's code and assigning an additional code to a credit history person. The document contains a list of the key particulars a credit history maker should indicate in his request to replace or cancel his code or assign a code or an additional code to him and the forms of CCCH letters in response to these requests.

The Bank of Russia issued Ordinance of August 31, 2005, No. 1611-U "On the Procedure and Forms of Presenting to Credit Bureaux Information Contained in Credit History Titles and Credit History Person Codes to the Central Catalogue of Credit Histories", which also established the procedures for using cryptographic protection in exchanges of electronic messages between the Bank of Russia and credit bureaux and the procedure for ensuring information security when using the cryptographic protection.

The Bank of Russia also issued Ordinance of August 31, 2005, No. 1612-U "On the Procedure for Requesting and Receiving Information from the Central Catalogue of Credit Histories by Credit History Persons and Users by Making a Requests to a Credit Institution" and Ordinance of November 29, 2005, No. 1635-U "On the Procedure for Making Requests and Receiving Information from the Central Catalogue of Credit Histories by a Credit History Person and User by Making a Request to a Credit History Bureau".

To keep credit institutions, credit bureaux and households informed and to facilitate the filing of inquiries by credit history persons and users to the CCCH, the Bank of Russia opened a CCCH section on its web site. It has inquiry forms which credit history persons and users who have a code or additional code can ask the CCCH for information about credit histories, change or cancel the credit history person code or establish an additional code. The CCCH section also provides the rules and regulations, technical characteristics of the forms of inquiry to the CCCH and other information.

To facilitate the electronic exchange between the CCCH and credit bureaux, credit institutions and credit history persons and users, the Bank of Russia developed and put in operation in 2005 the CCCH Automated System (CCCHAS), which made it possible to optimise the cost of collecting credit histories and receiving credit reports in the course of fulfilling their functions established by Federal Law 218-FZ. While preparing for the processing of credit history titles, the Bank of Russia tested the CCCHAS sub-system developed for exchange with credit bureaux.

III.9. Countering the Legalisation (Laundering) of Earnings Obtained in an Illegal Way and the Financing of Terrorism

In 2005, the Bank of Russia conducted substantial work to improve the methodology for countering money laundering and the financing of terrorism (AML/FT) by credit institutions and Bank of Russia regional branches, as well as to create conditions conducive to the effective implementation by credit institutions of AML/FT legislation.

The constant monitoring and analysis of credit institutions' statements and supervisory practices allowed the Bank of Russia to categorise the main types and signs of suspicious operations conducted by bank customers. Using the results of this work and seeking to prevent credit institutions from becoming involved in illegal activities and creating situations endangering the legitimate interests of depositors and creditors, the Bank of Russia issued letters in 2005 recommending credit institutions to tighten control over operations that might be connected with money laundering[74].

To upgrade internal controls in credit institutions, taking into account the experience gained and international standards, the Bank of Russia issued new methodological recommendations on the elaboration by credit institutions of internal control rules relating to AML/FT[75].

To provide methodological support to credit institutions, the Bank of Russia issued recommendations on the procedure for suspending and calculating suspension periods for individual types of cash operations[76] and two letters clarifying various aspects of the practical application of AML/FT laws.

While implementing the Agreement on Information Co-operation between the Central Bank of the Russian Federation and the Federal Financial Monitoring Service, carried out pursuant to the Federal Law "On Countering the Legalisation (Laundering) of Earnings Obtained in an Illegal Way and the Financing of Terrorism"[77], the Bank of Russia began to receive information in 2005 on the compliance by credit institutions with the requirements of this Law (hereinafter referred to as Federal Law No. 115-FZ). This information was widely used by the Bank of Russia for supervisory purposes.

Exercising the powers assigned to it by law to verify credit institutions' compliance with the requirements of Federal Law No. 115-FZ, the Bank of Russia inspected 797 credit institutions and/or their branches in the course of banking regulation and supervision[78] in 2005. The inspections focused on assessing the effectiveness of internal controls, including the quality and extent of the identification of customers and beneficiaries, the evaluation of the risk of customer involvement in money laundering, the consistency of the measures taken by a credit institution to detect suspicious operations conducted by its customers and the adequacy of the internal control rules to the specific activities of a credit institution.

The most typical drawbacks detected by inspections were: non-compliance with the requirements of Federal Law No. 115-FZ and Bank of Russia regulations regarding customer and beneficiary identification; collecting and documenting data on operations with money and other property subject to mandatory control and transactions which a credit institution has reason to suspect of being conducted for the purpose of money laundering and terrorist financing; and a failure to present this information to the authorised agency in time.

In taking decisions on using sanctions against credit institutions, the Bank of Russia made sure that the penalty was commensurate with the real level of the risk created by the shortcomings or violations of the AML/FT legislation committed by banks[79]. Implementing this policy, the Bank of Russia assessed the overall effect of the violations discovered by inspection and used corrective measures: informal measures, such as informing the management of credit institutions about the shortcomings detected in their work, and formal measures, such as ordering the credit institutions to rectify the faults discovered by inspectors,

[74] Bank of Russia Letter of January 21, 2005, No. 12-T "Methodological Recommendations on Tightening Control over the Purchase of Securities by Private Individuals for Cash and Purchase and Sale of Foreign Exchange"; Bank of Russia Letter of January 26, 2005, No. 17-T "On Tightening Control over Cash Operations"; Bank of Russia Letter of December 26, 2005, No. 161-T "On Stepping up Activity in Preventing Credit Institutions from Conducting Suspicious Operations".

[75] Bank of Russia Letter of July 13, 2005, No. 99-T "On Methodological Recommendations on Setting Internal Control Rules by Credit Institutions for the Purpose of Countering the Legalisation (Laundering) of Earnings Obtained in an Illegal Way and the Financing of Terrorism".

[76] Bank of Russia Letter of July 13, 2005, No. 97-T "On Methodological Recommendations the Suspension by Credit Institutions of Some Types of Cash Operations".

[77] This Agreement was signed on May 17, 2004.

[78] Bank of Russia Letter of April 6, 2005, No. 56-T "On Methodological Recommendations for Conducting Inspections of Credit Institutions to Verify Compliance with Federal Laws and Bank of Russia Regulations on Countering the Legalisation (Laundering) of Earnings Obtained in an Illegal Way and the Financing of Terrorism".

[79] Bank of Russia Letter of July 13, 2005, No. 98-T "On Methodological Recommendations on the Application of Bank of Russia Instruction of March 31, 1997, No. 59 'On the Use of Sanctions against Credit Institutions for Violation of Laws and Regulations on Countering the Legalisation (Laundering) of Earnings Obtained in an Illegal Way and the Financing of Terrorism'".

suspending or prohibiting individual banking operations, imposing fines and revoking banking licences.

The effect of AML/FT measures depends to a great extent on the qualifications of specialists in Bank of Russia regional branches and credit institutions. Under the Vocational Training Catalogue of Bank of Russia Staff, implemented in collaboration with specialists of the Ministry of the Interior and Federal Financial Monitoring Service, 12 seminars were held in 2005, which were attended by more than 540 managers and specialists with Bank of Russia regional branches. In October 2005, the Bank of Russia organised and held in collaboration with Russian banking associations and Deutsche Bank a conference on crucial issues and international standards related to AML/FT.

The measures taken in this field raised the banking community's awareness of the importance of AML/FT. Customer relations were improved, the quality and completeness of information were increased. According to available data, the Federal Financial Monitoring Service received in 2005 over 3 million reports on operations subject to mandatory verification and suspicious operations (1.7 million reports were received in 2004). About half of these reported suspicious operations conducted by customers. In addition, the share of communications that failed to pass the Federal Financial Monitoring Service's access control system because of message format errors made by credit institutions contracted by more than a half (from 10% in 2004 to 4.9% in 2005).

III.10. Co-operation with the Russian Banking Community

The Bank of Russia worked proactively with the banking community last year to draft rules and instructions on banking regulation and supervision.

The Bank of Russia put on its web site for discussion with the banking community the Draft Ordinance "On the Reduction of a Bank's Credit Risk for Economically Connected Borrowers" and the Draft Instruction "On Setting Limits on Open Currency Positions, the Methods of Calculating them and the Specifics of Supervision of their Observance by Credit Institutions". The Bank of Russia took into account the criticism and proposals sent to the Bank of Russia by the banking community, including the Association of Russian Banks and the Association of Regional Banks of Russia, when finalising these two documents.

In addition, the Bank of Russia held consultations with the Russian banking community on a number of issues relating to the improvement of risk management, such as:

— the regulation of credit institutions' operations with American Depositary Receipts;
— loss provisioning with due account of collateral;
— techniques of creating portfolios of homogeneous claims;
— problems of determining liquid assets;
— calculation of required ratios;
— improving market-risk regulation.

The Bank of Russia put the draft of its Letter "On the Contemporary Standards of Corporate Governance in Credit Institutions" on its official web site for public debate. Comments and proposals made by credit institutions and banking associations when the draft was being discussed were also placed on the Bank of Russia official web site.

In addition, the Bank of Russia considered proposals made by the Association of Russian Banks to amend the Federal Law "On Advertising" with a view to regulate the contents of banking service advertisements. The Bank of Russia proposed establishing a requirement that an advertisement containing information on the terms and conditions of an agreement should not omit mention of any substantial term or condition of this agreement.

The Bank of Russia also considered the comments and proposals made by the Association of North-Western Banks on the draft Federal Law "On Consumer Credit", which pointed to the need to rethink the concept of the law and include in it the provision to the effect that banks must inform their customers about additional expenses that may be involved in a loan.

The Bank of Russia organised and hosted the 14th International Banking Congress, which took place in St Petersburg on June 1 to 4, 2005, under the title "Banks. Regulation. Economics". Representatives of Russian and foreign political and business circles, international organisations, foreign central (national) banks and supervisory authorities and the banking community attended.

The Congress discussed current trends in banking sector development, such as the increased functional role of the banking sector in economic development, the government policy of strengthening the banking sector, the establishment of the deposit insurance system, key problems of banking regulation in Russia, international experience in upgrading the banking sector's infrastructure and prospects for emulating this experience in Russia, the economic and legal aspects of relations between the Bank of Russia and credit institutions and interaction of science and banking. After the discussion, the Congress adopted recommendations on the development of Russia's banking system.

III.11. Cooperation with International Financial Organisations and Foreign Central Banks and Regulatory Authorities in the Field of Banking Supervision

Bank of Russia representatives participated in working meetings, consultations and the drafting of documents and comments within the framework of the ***International Monetary Fund (IMF)*** mission of experts in the Bank of Russia. These documents and comments dealt with, among other things, capital adequacy, stress testing and the updating of the Financial Sector Assessment Programme.

The Bank of Russia co-operated with IMF technical assistance advisors, who gave advice on the international expertise in banking and banking supervision.

Within the framework of the IMF Coordinated Compilation Exercise for Financial Soundness Indicators, Bank of Russia employees participated in a regional meeting of FSI coordinators and compilers, held in Vienna on May 9 to 13, 2005, which discussed both common and country-specific problems involved in compiling metadata.

The Bank of Russia cooperated with the ***World Bank*** in implementing the Financial Institution Development Project, which was completed on December 31, 2005.

The Bank of Russia provided organisational support to the ***International Finance Corporation (IFC),*** which is a part of the World Bank Group, in holding seminars for bankers in the Siberian, Ural, Central, Southern, Volga and Far Eastern Federal Districts, organised by the IFC under the project "Corporate Governance in the Russian Banking Sector".

Bank of Russia representatives contributed to the activities (making proposals and comments on draft documents, providing information and participating in sessions) of the Basel Committee's working groups (Core Principles Liaison Group and Working Group on Capital) and its regional groups (Group of Banking Supervisors from Central and Eastern Europe and Transcaucasia, Central Asia and Russian Federation Regional Group for Banking Supervision) and also the Working Group of Supervisory Authorities Heads for Basel Committee on Banking Supervision and Supervisory Board of FSI Connect.

During the year Bank of Russia representatives attended the seminars on banking supervision held by the ***Financial Stability Institute*** of the Bank for International Settlements and Basel Committee on Banking Supervision.

Andrei Kozlov, Bank of Russia First Deputy Chairman, participated in the ***Bank for International Settlements*** Governors Meeting on the banking systems in countries with transitional economies.

The Bank of Russia optimised and upgraded prudential reporting practices within the framework of EU/TACIS Banking Supervision and Reporting Project, implemented by the ***European Union*** to improve banking supervision and establish a system of prudential reporting based on the IFRS and to incorporate international best practice[80]. While implementing the Project, the Bank of Russia proposed a new architecture of prudential reporting in compliance with risk-based banking supervision and international best practice and designed to make the current reporting forms more informative and helpful for supervisors, as well as to update the content and procedure for compiling and presenting them.

Bank of Russia representatives participated in the 101st meeting of the Financial Market Committee of the ***Organisation for Economic Cooperation and Development (OECD),*** which discussed financial policy, financial regulation and economic growth and the Basel Committee's draft consultative document "Enhancing Corporate Governance for Banking Organisations".

Cooperation with foreign supervisory authorities

In 2005, the Bank of Russia made vigorous efforts to draft, deliver and agree the texts of agreements on cooperation (memorandums of understanding) in the field of banking supervision with 21 foreign supervisory authorities.

The Bank of Russia took part in a meeting of supervisors of the 12-nation European Economic Area, held in Helsinki on October 20 and 21, 2005, which discussed the legal aspects of cooperation in banking supervision, including information exchange and on-site inspections.

As a result of work completed in 2005, the Bank of Russia signed new agreements on cooperation and memorandums of understanding in banking supervision with the following banks and supervisory authorities:

— National Bank of the Republic of Belarus (October 7, 2005);
— Bank of Lithuania (October 24, 2005)
— China Banking Regulatory Commission (November 3, 2005).

In addition, the Bank of Russia conducted negotiations on cooperation in banking supervision with a number of countries, including OECD members in 2005.

The Bank of Russia also cooperated with foreign central banks and supervisory authorities in personnel training. Within the EU/TACIS project "Central Bank Training — III", which was completed in October 2005, the Bank of Russia cooperated:

— with the Institute of Certified Accountants of Ireland (Dublin, April);

[80] The Bank of Russia implemented this project from 2003 to 2005.

— with the Bank of Finland on assessing risk management and internal controls and their adequacy to the nature and scale of the activities of credit institutions and banking groups (Finland, June) and financial stability analysis in the Bank of Finland (Finland, August).

The Bank of Russia continued to participate in the work of the ***Sub-group of Banks/Financial Services of the Russian-German Intergovernmental Working Group on the Strategy of Economic and Financial Cooperation.***

In January 2005, it organised and held a meeting on the financing of small and medium-sized enterprises in the German Ministry of Finance in Berlin.

In addition, the Bank of Russia organised and hosted a meeting of a subgroup on venture capital in its St Petersburg branch in November 2005.

It took part in training programmes on the supervision of problem banks and internet banking, organised by the ***Financial Services Volunteer Corps (FSVC)*** in conjunction with the US Office of the Comptroller of the Currency (in July and September 2005 respectively) and in the international seminar “Financial Stability: the Role for Central Banks” for members of the ***Central Asia, Black Sea and Balkan Central Banks Club,*** held in Tula on December 13 and 14, 2005.

Pursuant to paragraphs 52 and 53 of the agreements on the creation of a ***Single Economic Space (SES),*** the Bank of Russia and the Deposit Insurance Agency and experts from Belarus, Kazakhstan and Russia continued to draft agreements on the harmonisation of their deposit insurance systems and banking laws in accordance with the Basel principles (July 5 to 8, 2005, and December 15 and 16, 2005, Moscow).

Within the framework of the ***Eurasian Economic Community (EurAsEC),*** the Bank of Russia took part in the following meetings of the Central (National) Bank Governors Council of the EurAsEC Treaty:

— the 12th meeting of the Central (National) Bank Governors Council on upgrading credit institutions’ reporting forms used for supervision and on the procedure for supervising banking groups on a consolidated basis, held in Moscow;

— the 13th meeting of the Central (National) Bank Governors Council on a draft procedure for supervising banking groups on a consolidated basis and on the upgrading of credit institutions’ reporting forms used for supervision, held in Almaty, Kazakhstan.

Bank of Russia representatives participated in an international seminar on urgent problems of banking supervision, organised for the EurAsEC central (national) banks and held in Tula on September 26 to 30, 2005.

Within the framework of the ***Interbank Currency Council of the Central Bank of the Russian Federation and National Bank of Belarus,*** Bank of Russia representatives helped prepare materials and attended the following meetings of the Interbank Currency Council:

— the 20th meeting on progress in establishing common principles of conducting banking operations and accounting and reporting in the Russian and Belarus banking systems, compatible with international financial reporting standards, held in Grodno;

— the 21st meeting on signs of financial instability in the Belarusian banking system, which can indicate an imminent systemic banking crisis in Belarus, held in Astrakhan;

— the 22nd meeting on progress in bringing national banking supervision practices into conformity with the recommendations of the Basel Committee on Banking Supervision.

The Bank of Russia organised meetings with representatives of foreign financial institutions — ***Merrill Lynch, Barclays Capital, HSBC and Deutsche Bank*** — to discuss the international practice of including subordinated financial instruments in the capital calculation and the possibility of using such instruments by Russian credit institutions. The international practices discussed during these meetings were taken into account in drafting amendments to the Federal Law “On the Insolvency (Bankruptcy) of Credit Institutions” and the Federal Law “On the Central Bank of the Russian Federation (Bank of Russia)”. These amendments are designed to create a legal framework for the further conversion of the Russian practice of including subordinated loans in the own funds (capital) calculation to internationally accepted banking capital calculation standards.

III.12. Outlook for Banking Regulation and Supervision in Russia

In 2006, the Bank of Russia will take practical steps to accomplish the tasks set in the Russian Banking Sector Development Strategy until 2008, to increase the banking sector stability and protect the interests of creditors and depositors.

This work will be carried out in the following areas.

Decision-making in respect to the state registration of credit institutions and licensing of banking activities

In 2006, the Bank of Russia will continue to propose amendments to banking legislation to create equal notification conditions for residents and non-residents (more than 1% of authorised capital) and obtaining Bank of Russia prior permission (more than 10% of authorised capital) for the acquisition of shares (stakes) in credit institutions. This standard will help the Bank of Russia tighten control over the quality of bank capital formation, the financial standing of investors and the transparency of the ownership structure of credit institutions.

While implementing the Strategy, the Bank of Russia will continue to refine the draft law amending the Federal Laws "On Banks and Banking Activities" and "On the Central Bank of the Russian Federation (Bank of Russia)" with a view to specify the requirements for executives and members of the board of directors (supervisory board) and grant the Bank of Russia the power to set criteria of their business reputation. Specifically, the draft law provides for:

— the right of the Bank of Russia to establish additional fitness and propriety requirements of persons holding executive positions and members of the board of directors (supervisory board) (they must have a higher education and a good track record in executive positions) and the right to set criteria for their business reputation. These requirements conform with international standards and were recommended by IMF and World Bank experts in 2003 when the Financial Sector Assessment Programme (FSAP) for Russia was implemented (Article 16 of the Federal Law "On Banks and Banking Activities" and Article 60 of the Federal Law "On the Central Bank of the Russian Federation (Bank of Russia)";

— precluding individuals found to have caused the bankruptcy of a credit institution in which they held a large block of shares (a stake of more than 10%) becoming members of the board of directors (supervisory board) or taking up an executive position (Article 16 of the Federal Law "On Banks and Banking Activities");

— establishing the procedure for obtaining prior approval of the candidates for the membership of the board of directors (supervisory board) (Article 11.1 and Article 14 of the Federal Law "On Banks and Banking Activities");

— compliance with fitness and propriety requirements by candidates to executive positions and members of the board of directors (supervisory board) of a credit institution during their entire term of office in accordance with the international practice of banking supervision and Principle 3 of the Basel Committee's Core Principles for Effective Banking Supervision (Article 11.1 of the Federal Law "On Banks and Banking Activities");

— the right of the Bank of Russia to refuse permission for the acquisition of more than 10% of shares (stakes) in a credit institution if the acquirer does not meet fitness and propriety requirements (Article 11 of the Federal Law "On Banks and Banking Activities" and Article 61 of the Federal Law "On the Central Bank of the Russian Federation (Bank of Russia)";

— broadening the powers of the Bank of Russia to receive information on the financial position and business reputation of the acquirers of shares (stakes) and founders (members) (Article 61 of the Federal Law "On the Central Bank of the Russian Federation (Bank of Russia)";

— criteria for identifying the real owners of credit institutions and the procedure for disclosing information about them.

Amendments are to be made in banking legislation in 2006:

— to improve procedures for reorganising credit institutions by merger, acquisition or reorganisation. The draft federal law amending the Federal Law "On Banks and Banking Activities" aims to create legal conditions for simplifying bank reorganisation procedures and increasing the protection of the interests of creditors of reorganised credit institutions. The principal measures to be implemented for this purpose are:

— to simplify the procedure for notifying the creditors of a reorganised credit institution. The credit institution is no longer required to notify each creditor in writing. The creditor notification procedure is established by the board of directors of the reorganised credit institution;

— to ensure transparency of the reorganisation procedure, a credit institution must disclose information about significant facts (events or actions) affecting its financial and economic activities from the day the decision to reorganise is taken to the end of the reorganisation by publishing this information in a period-

ical. A list of these facts (events or actions) is to be established by law;
- to ensure that the acquiring credit institution or the credit institution established as a result of a merger or reorganisation retains its liquidity and solvency, it shall be stipulated by law that only individual creditors will have the right to demand an early fulfilment of pecuniary obligations, if these obligations arose before the credit institution announced the reorganisation date. Corporate creditors' claims for an early fulfilment of obligations should only be met if this is stipulated by the term and conditions of an agreement;
- to establish the minimum own funds (capital) of an operating bank at the ruble equivalent of 5 million euros.

A minimum authorised capital is to be established for new credit institutions and own funds (capital) for banks applying for a general licence.

In addition, pursuant to paragraph 40 of the Strategy, the capital of operating credit institutions is to be at least 5 million euros in ruble terms as of January 1, 2007. Banks that have a smaller capital by this date will be able to remain in operation if their own funds (capital) do not decrease below the level reached at the said date (the "grandfather clause")[81].

These requirements will create favourable conditions for the further development of the banking system, including regional banks, and make it possible to set targets for the capitalisation of banks, which is a major factor in banking sector development and stability.

Pursuant to Article 35 of the Federal Law "On Banks and Banking Activities" and realising the need to overhaul (in connection with the coming into force of Federal Law No. 173-FZ "On Foreign Exchange Regulation and Control") the procedure for issuing permits to credit institutions to participate in non-resident capital, established by Bank of Russia Regulation of April 29, 1998, No. 27-P "On the Procedure for Granting Permits by the Central Bank of the Russian Federation to Banks to Participate in the Authorised Capital of Credit Institutions Abroad", the Bank of Russia is to establish a procedure for granting permits to credit institutions to open subsidiaries in other countries and to acquire the status of the parent company with regard to non-resident corporate entities.

As interest in operations with shares issued by Russian credit institutions on organised markets and (or) by public offering is growing and financial derivatives (depositary receipts) programmes of Russian issuers, including banks, are expanding, the Bank of Russia understands that bank share placement and circulation procedures need to be eased. This would help increase the capitalisation of credit institutions and the banking sector as a whole. The Bank of Russia's efforts aim to cut the costs involved in fulfilling of the duties established by the regulator without abandoning the principle of materiality in controlling the quality of banks' capital, the financial position of investors and the transparency of a bank's ownership structure.

To establish the procedure and criteria for assessing the persons appointed to executive positions in a credit institution or its branch and elected to the board of directors (supervisory board) of a credit institution to make sure that they meet fitness and propriety requirements set by the Federal Law "On Banks and Banking Activities", the Bank of Russia will continue work in 2006 on the draft Ordinance "On the Fitness and Propriety Requirements Established by the Bank of Russia for Candidates to Executive Positions in a Credit Institution or its Branch and Persons Elected to the Board of Directors (Supervisory Board) of a Credit Institution". For the same purpose it will continue work on the draft Letter "On the Procedure for Assessing by Bank of Russia Regional Branches the Business Reputation of Candidates to Executive Positions in a Credit Institution or its Branch and Persons Elected to the Board of Directors (Supervisory Board) of a Credit Institution".

Banking regulation and off-site supervision

The activities of the Bank of Russia in off-site banking supervision in 2006 will aim to develop risk-based supervision of credit institutions by upgrading the banking regulation system and the methods for assessing the financial soundness of credit institutions, improving the quality of analysis and the promptness of supervisory response. It will also seek to introduce into supervisory practice the "know-the-bank-and-its-customers" principle, develop the early warning system designed to detect banks' problems at the early stages and to make additional demands on the quality of the intrabank risk management and internal controls.

The Bank of Russia will continue to pursue measures designed to promote the substantive approach to supervision and increase the accuracy of assessing the financial standing of credit institutions. To create more favourable conditions for substantive supervision, legislative amendments should be made, establishing the powers

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[81] Under Federal Law of May 3, 2006, No. 60-FZ "On Amending the Federal Law 'On Banks and Banking Activities'" and the Federal Law "On the Central Bank of the Russian Federation (Bank of Russia)":
- the minimum authorised capital for a newly registered bank is established at the ruble equivalent of 5 million euros and the minimum authorised capital for a newly registered non-bank credit institution is set at the ruble equivalent of 500,000 euros;
- a general licence for banking operations may be granted to a credit institution with own funds (capital) of no less than the ruble equivalent of 5 million euros;
- own funds (capital) of a non-bank credit institution seeking the status of a bank should be no less than the ruble equivalent of 5 million euros;
- the minimum own funds (capital) for a bank are set at the ruble equivalent of 5 million euros. A bank that has own funds (capital) of less than the ruble equivalent of 5 million euros as of January 1, 2007, will be able to continue operations provided that its own funds (capital) do not decrease from the level reached at January 1, 2007.

of the Bank of Russia in using professional judgement in supervisory practice.

In collaboration with the Ministry of Finance, the Bank of Russia is to complete the drafting of amendments to the laws “On Banks and Banking Activities” and “On the Central Bank of the Russian Federation (Bank of Russia)”, legitimising the main aspects of consolidated supervision.

There are plans to improve the methodologies for assessing the financial soundness of credit institutions and differentiate the supervisory regimes, depending on the financial condition of credit institutions, their management and the transparency of their ownership structure. For this purpose, the Bank of Russia is to complete the drafting of the Regulation “On the Assessment of Financial Soundness of a Credit Institution”, based on the standards which are now used in establishing banks’ compliance with the deposit insurance system access requirements by pronouncing a professional judgement in assessing a credit institution’s risks. The new financial soundness assessment system is designed to eliminate substantial differences in financial soundness evaluation practices for banking supervision purposes and for establishing whether a bank is financially stable to participate in the deposit insurance system.

To this end, the Bank of Russia has drafted the Regulation “On the Regimes of Supervision of Credit Institutions”, which stipulates that the supervisory tactic with regard to a credit institution should depend on the assessment of its financial soundness and supervisory decision-making should rest upon the professional judgement.

In 2006, the Bank of Russia will continue to upgrade its methodologies for assessing the financial stability of the banking sector as a whole and the soundness of individual credit institutions, including stress-testing methodology. It will establish a financial stability monitoring system, which in addition to the liquidity, non-financial corporation credit risk and consumer lending risk monitoring subsystems already in operation, will be supplemented with market risk and capital adequacy monitoring subsystems. The Bank of Russia will continue to upgrade the current non-financial corporation monitoring system with the aim of adding an element to the early warning system that will alert supervisors about the risks connected with the deterioration of the financial condition of non-financial corporations.

The Bank of Russia will continue to calculate in 2006 financial soundness indicators (FSIs) within the framework of the IMF Coordinated Compilation Exercise for Financial Soundness Indicators. The final version of metadata and FSIs calculated as of December 31, 2005, will be available on the IMF web site. The number of FSIs will be increased as other agencies become involved in the project. The Russian banking sector’s macroprudential indicators published by the Bank of Russia will also be harmonised with internationally accepted standards.

To improve banking legislation, the Bank of Russia will participate in drafting amendments to the Federal Law “On the Central Bank of the Russian Federation (Bank of Russia)”, designed to improve the regulation of risks assumed by credit institutions when conducting credit operations and transactions with a group of economically related borrowers and borrowers connected with the credit institution.

Taking into consideration the banking community’s proposals and criticism, the Bank of Russia will continue work on amendments to its Instruction of January 16, 2004, No. 110-I “On Banks’ Prudential Ratios”, setting a limit (N6.1 ratio) on maximum credit risk per group of economically connected borrowers.

To improve the methodologies used by credit institutions while conducting operations as well as banking regulation and supervision, the Bank of Russia will continue to draft proposals in 2006 on revising the principles of regulating liquidity risk taking into account the results of EU/TACIS Project “Banking Supervision and Reporting”.

It plans to issue an instruction on banking operations and transactions conducted by settlement non-bank credit institutions, on the prudential ratios for settlement non-bank credit institutions and the specifics of the Bank of Russia oversight in this area, to replace Bank of Russia Regulation of September 8, 1997, No. 516 “On the Prudential Regulation of Non-Bank Credit Institutions Conducting Settlement Operations and Collection Organisations”. The instruction will list the operations and transactions non-bank credit institutions may and may not conduct. It will also list the financial instruments in which settlement non-bank credit institutions can invest their spare funds and will grant to settlement non-bank credit institutions the right to extend credit to settling participants on their own behalf and at their own expense within the limits of a liquidity fund. In addition, the document will optimise the list and methods for calculating the prudential ratios for settlement non-bank credit institutions.

To improve the methodology for making by credit institutions loan loss provisions and provisions for loan debts and similar debts, the Bank of Russia, taking into account the experience gained in using this methodology, will amend Regulation No. 254-P to revise the types of collateral, cancel the collateral insurance requirement and review the loan portfolio provisioning methodology in the context of IAS 39.

The Bank of Russia will issue recommendations on some aspects of loan quality evaluation, which take into account the supervisory experience of Bank of Russia regional branches.

It will continue to phase in the Basel Committee’s New Capital Accord (Basel II). Specifically, the Bank of Russia will amend Instruction No. 110-I to revise the capital adequacy ratio calculation (N1 ratio) procedure in the context of its plans to introduce a Simplified Standardised Approach.

The Bank of Russia will complete the drafting of amendments to the Federal Laws “On Insolvency (Bankruptcy) of Credit Institutions” and “On the Central Bank of the Russian Federation (Bank of Russia)”, which will create legal conditions conducive to the further conversion of Russian own funds (capital) calculation rules to internationally accepted standards.

There are plans to draft recommendations on interest risk management in credit institutions, setting the principles and methods for managing and calculating interest rate risk in respect to financial instruments that are susceptible to changes in interest rates and not included in a credit institution's trade portfolio.

The Bank of Russia also plans to issue the following recommendations:

— on the assessment by Bank of Russia regional branches of the quality of corporate governance in credit institutions and the state of internal controls in credit institutions and banking groups;
— on the self-assessment by credit institutions of the quality of corporate governance and the state of legal and reputation risk management;
— on the management of risks associated with internet banking;
— on the assessment of information technologies used by credit institutions;
— on Bank of Russia regional branches' monitoring of the contents of credit institutions' web sites to detect information indicating that a credit institution is involved in illegal activities or activities endangering the legitimate interests of its creditors and depositors and banking sector stability and on the prompt supervisory response to such actions.

The Bank of Russia is continuing to work on the concept of a law that will grant it the right to supervise corporate entities providing services to credit institutions relating to banking operations and other transactions via telecommunications systems and the internet and computer service providers of credit institutions.

The Bank of Russia is to participate in drafting a law to amend Article 5 of the Federal Law "On Banks and Banking Activities" for the purpose of legitimising the establishment of general bank management funds (OFBUs). The amendments will enable credit institutions to set up OFBUs, which they now manage in accordance with Bank of Russia Instruction of July 2, 1997, No. 63 "On the Procedure for Conducting Trust Management Operations and their Accounting by Russian Credit Institutions" and establish the regulatory powers of the Bank in respect to the OFBUs. The draft law will also establish some terms and conditions of an OFBU trust management agreement, including its time frames, the liability of a trustee and risks associated with the devaluation of property put in trust.

The Bank of Russia is to participate in drafting laws designed to encourage the securitisation of bank assets.

Amendments are to be made to the laws "On Banks and Banking Activities" and "On the Central Bank of the Russian Federation (Bank of Russia)" to increase the role and responsibility of the board of directors (supervisory board) of a credit institution. They will also detail the matters within its exclusive competence and include in the charters of credit institutions requirements for the make-up of the board of directors, such as the requirement to have a number of independent (non-executive) directors on the board.

Amendments are to be made to the laws "On Banks and Banking Activities" and the "On the Central Bank of the Russian Federation (Bank of Russia)" to give the Bank of Russia the powers to assess the quality of management in credit institutions and take supervisory action against them if necessary.

In addition, the Bank of Russia intends to complete methodologies for the purpose of introducing the institution of curatorship in Russian supervisory practice. Specifically, it is drafting the Bank of Russia Regulation "On the Curator of a Credit Institution" and the Methodological Guidance for the Curator (known as "The Curator's Handbook"). The latter is being drafted to help curators and other employees of Bank of Russia regional branches collect and systematise data on credit institutions. It will also help them analyse and evaluate credit institutions' activities on the basis of professional judgement about various aspects of their activities, the current state of and prospects for their financial soundness and the quality of governance and internal controls.

To optimise and upgrade supervisory reporting, the Bank of Russia plans to draft amendments in 2006 to the current package of prudential statements, based on expert recommendations made while implementing the EU/TACIS Project, and hold an all-round discussion of new and revised forms of statements with the Russian banking community before putting them into supervisory practice.

While reducing the number of reporting forms and procedures, the Bank of Russia will promote the use of the internet by credit institutions in reporting to the Bank of Russia, which will make it possible to preclude the overlapping of incoming data and allow credit institutions to cut costs.

As part of a project to develop a Bank of Russia's unified information system for banking sector regulation and development, the Extranet Portal information system is to be installed in the Bank of Russia Moscow Branch. One purpose of this system is to arrange an exchange of information between the Bank of Russia and credit institutions. The system will help collect data reported by credit institutions, using a single computer centre and standard formats, and keep the banking community informed on issues relating to the formatting and presenting statements electronically.

In 2006, the Bank of Russia will continue to develop the unified information system for banking sector regulation and development. It plans to organise a single database for credit institutions' statements and other data, begin the development of information subsystems for analysing information from a unified database and standardise the formats of collecting statements from credit institutions and their branches.

To streamline, optimise and structure banking statistics indicators and thus upgrade the current system of data collection, processing, storage and utilisation in the Bank of Russia in line with Bank of Russia Regulation of March 14, 2005, No. 267-P work will continue to originate a Catalogue of Banking Statistics Indicators.

Household deposit insurance in Russian banks

To improve the deposit insurance system, the Bank of Russia will continue to draft amendments in 2006 to Article 11 of the Federal Deposit Insurance Law and Article 6 of the Federal Law “On Bank of Russia Payments on Household Deposits with Bankrupt Banks Uncovered by the Deposit Insurance System”.

The amendments increase the level of compensation paid out on deposits by the Deposit Insurance Agency to 190,000 rubles. The following compensation payment procedure will be established: full compensation will be paid on deposits of up to 100,000 rubles and any amount in excess of 100,000 rubles will be compensated for by 90%, but the maximum compensation payment on a deposit will be 190,000 rubles. At the same time, to protect depositors of banks outside the deposit insurance system and guarantee them equal conditions with depositors of the banks registered with the system, an amendment is to be made to the Federal Law “On Bank of Russia Payments on Household Deposits with Bankrupt Banks Uncovered by the Deposit Insurance System” to provide for a commensurate increase in Bank of Russia compensation payments to depositors of these banks.

In addition, to improve the deposit insurance system, the Bank of Russia will continue to draft amendments to the Federal Deposit Insurance Law and other federal laws for the following purposes:

— to upgrade the criteria of and procedures for verifying how banks comply with the deposit insurance system requirements;
— to revise the procedures ensuring the effectuation of insurance payments, including payments to individual categories of depositors;
— to bring the functions and powers of the Deposit Insurance Agency, established by the Deposit Insurance Law, into conformity with the Federal Laws “On the Insolvency (Bankruptcy) of Credit Institutions” and “On Banks and Banking Activities” (in respect to the functions of the receiver (liquidator) of banks).

Banks that held a licence to take household funds on deposit when the Deposit Insurance Law came into force but refused to participate in the deposit insurance system in 2004 will have the right to ask the Bank of Russia to admit them in 2006. Therefore, the Bank of Russia will implement the procedures connected with the examination of such requests (if there are any).

On-site inspection

Under the Summary Plan of Comprehensive and Selective Inspections of Credit Institutions and their Branches 1,463 inspections will be conducted in 2006, of which 844 will be of credit institutions and 619 of credit institutions’ branches. Comprehensive inspections are to be conducted in 338 credit institutions and 103 of credit institutions’ branches and 151 inspections are to be conducted with the participation of Deposit Insurance Agency employees.

When conducting scheduled inspections of credit institutions, Bank of Russia authorised representatives will pay particular attention to:

— credit institutions’ complying with the requirements of the Federal Law “On Countering the Legalisation (Laundering) of Earnings Obtained in an Illegal Way and the Financing of Terrorism”;
— the effectiveness of internal controls;
— assessing credit risk and risk management systems;
— evaluating of the reliability of accounting and reporting;
— how credit institutions implement measures to rectify the faults (shortcomings) detected by the previous inspection;
— examining deposit operations;
— verifying compliance with the requirements of the Federal Deposit Insurance Law;
— assessing the financial condition of a credit institution and its prospects for the future;
— settlement discipline;
— cash discipline;
— how credit institutions observe foreign exchange legislation.

Risk-based supervision requires supervisors to pay heightened attention to new risks caused, among other things, by a rapid increase in consumer lending, operations with discounted promissory notes and long-term lending. Since these and other new objectives of supervision and inspection require appropriate methodological and legislative support, the Bank of Russia will continue to draft proposals for upgrading the methodological and legal framework of supervision and inspection.

To make inspections more effective, preparations for them need to be improved to establish the targets of inspection more accurately. Therefore, the Bank of Russia will continue to attach great importance to analysis: the main questions included in the assignment for inspection will be formulated on the basis of an analysis of the reports on the previous inspections and off-site supervision materials. In 2005, the Bank of Russia prepared and sent to regional branches analytical materials designed to help regional inspections units improve preparations for inspections (materials are regularly sent to the interregional inspectorates and Bank of Russia regional branches).

To improve the quality of inspection materials, the Bank of Russia will continue the time-tested practice of analysing individual inspection reports, discussing them and making recommendations on how to improve them. These recommendations are made known to the inspection divisions of the Main Inspectorate for Credit Institutions and Bank of Russia regional branches.

The introduction of advanced communications and software will help improve inspection. New technology and software allow to improve analysis and optimise statements banks send to the Bank of Russia. For this purpose, 75 Bank of Russia regional branches are continuing to test run the computer-based Automated Inspection System, which collects all data on inspections in real time and enables a user to obtain them in any form, including approved reporting forms.

Financial rehabilitation and liquidation of credit institutions

To accomplish the objectives set in the Strategy to prevent the insolvency (bankruptcy) of credit institutions, the Bank of Russia will continue to use measures against credit institutions provided by the Federal Law "On the Insolvency (Bankruptcy) of Credit Institutions". It will seek to improve the procedures on preventing a credit institution's bankruptcy quickly and in good time, detecting problems in a credit institution in the early stages to prevent any further deterioration and ensuring that the owners of credit institutions take bankruptcy prevention measures in time.

Another priority for the Bank of Russia is to upgrade bank liquidation procedures. Measures include creating an effective mechanism to sell the assets of liquidated banks, making the liquidation procedures more transparent, meeting creditors' and depositors' claims to a fuller extent and increasing the responsibility of a receiver (liquidator). The Bank of Russia will oversee the activities of receivers (liquidators) by analysing monthly reports and other data presented by liquidated credit institutions.

The Bank of Russia will continue to implement the provisions of the Federal Law "On Bank of Russia Payments on Household Deposits with Bankrupt Banks Uncovered by the Deposit Insurance System".

To improve applicable legislation, the Bank of Russia will examine draft laws designed to enhance the effectiveness of and strengthen the collateral system and draft proposals on legislation aimed at preventing illegal transactions conducted shortly before a bank goes insolvent (bankrupt) and asset diversion. Specifically, it will propose a simpler procedure for disputing dubious transactions concluded by a credit institution shortly before going bankrupt and impose tougher penalties on bank managers for the forgery and destruction of documents.

To implement the provisions of the bank bankruptcy legislation, the Bank of Russia plans to issue the following regulations in 2006:

— on the specifics of conducting settlement operations by credit institutions after the revocation (cancellation) of their banking licence and on the accounts used by receivers (liquidators and liquidation commissions);
— the relationship between Bank of Russia regional branches and credit institutions whose banking licences have been revoked;
— Bank of Russia inspection of the activities of credit institutions' receivers (liquidators).

Pursuant to Article 50.42 of the Federal Law "On the Insolvency (Bankruptcy) of Credit Institutions", the Bank of Russia will continue to draft a new version of its Regulation "On the Procedure for Compiling and Presenting an Interim Liquidation Balance Sheet and Liquidation Balance Sheet of a Credit Institution and Approving them by a Bank of Russia Regional Branch". The reports on the main activities of the agency liquidating a credit institution and thereby allowing an assessment of the entire liquidation process are to include indicators on the stocktaking and evaluation of property (assets) of a credit institution, the safety of this property (assets), the results of property sale, the funds at the disposal of a receiver (liquidator) and how they have been used on current expenses and meeting creditors' claims. When drafting the Regulation, the Bank of Russia took into account the experience of regional branches in overseeing the liquidation of credit institutions.

Countering the legalisation (laundering) of earnings obtained in an illegal way and the financing of terrorism

To implement the Strategy and help prevent credit institutions from being used for illegal purposes, especially terrorist financing and money laundering, the Bank of Russia will proactively participate in 2006 in amending the Federal Law "On Countering the Legalisation (Laundering) of Earnings Obtained in an Illegal Way and the Financing of Terrorism". These amendments aim to lift restrictions on the inspection of credit institutions to verify their compliance with the requirements of AML/FT laws and establish grounds for terminating a bank account (deposit) agreement by a credit institution.

To help ensure that credit institutions strictly comply with the requirements of AML/FT laws and build upon the law enforcement practice, the Bank of Russia will improve further the AML/FT regulations and provide credit institutions with methodologies for detecting operations requiring close scrutiny.

While fulfilling its supervisory functions to ensure credit institutions' compliance with the requirements of AML/FT laws, the Bank of Russia will focus on evaluating internal controls in credit institutions to make sure that they effectively combat money laundering and terrorist financing.

The development of the Central Catalogue of Credit Histories

The Bank of Russia will continue in 2006 to agree with the corresponding federal executive authorities the regulations it drafted on the procedure for making inquiries and receiving information from the Central Catalogue of Credit Histories by a credit history person and user by mail and through notaries.

After the credit bureau is put on the State Register of Credit Bureaux in 2006, the CCCH will begin to receive the titles of credit histories from credit bureaux and provide information on credit bureaux at the request of credit history person and users.

Annexes IV

IV.1. Formation of banking sector stability monitoring system

Implementing the legislatively established objective of developing and strengthening the Russian banking system, the Bank of Russia is elaborating the methodologies and tools to monitor the banking sector stability. The operating banking sector stability monitoring system is comprised of three subsystems:

- monitoring the risk of lending to non-financial corporations;
- monitoring the risk of consumer lending;
- monitoring liquidity.

The Bank of Russia is continuing to develop the market risk and capital adequacy monitoring subsystems.

The choice of indicators used in monitoring financial stability depends on the content of credit institutions' reporting. The reports of the 200 largest banks (by assets) are analysed in the course of monitoring[82]. For the purposes of analysis, these banks are divided into the following subgroups: the Moscow-based banks, regional banks and banks controlled by foreign capital.

To determine the threshold values that might indicate banking sector problems if they are exceeded, the indicators used in the corresponding monitoring subsystems are zoned. The indicator zoning depends on the level of danger to banking sector stability (the traffic lights principle):

- the green zone means that there are no problems;
- the yellow zone indicates that unfavourable trends may evolve in a bank;
- the red zone means that imminent problems may emerge.

When individual banks are scrutinised within any of the said subsystems, the risk group to which other monitoring subsystems assign the bank are also considered.

Credit risk monitoring subsystems: the risk of lending to non-financial corporations and the risk of lending to households

Credit risk monitoring is based on the calculation of the adjusted capital adequacy ratio, which is determined by using own funds (capital) reduced by possible losses reflecting the corresponding risks. The following assumptions are made in calculating the adjusted capital adequacy ratio:

- losses from non-performing loans are assumed to be equal to overdue debt on these loans;
- a bank's own funds (capital) are reduced by these losses (overdue debt net of the provision made for loan losses, loan debts and similar debts).

Regulatory capital adjusted in the manner is used in calculating the adjusted capital adequacy ratio.

To identify *particular banks* in which non-performing loans may reduce capital adequacy to a dangerously low level (less than 12%), the Bank of Russia analyses the adjusted capital adequacy ratio taking into account the real level of overdue debt.

The main credit risk indicator used for the *200 largest banks and the groups of banks* is the share of overdue debt in total credit to non-financial corporations or households.

To determine the threshold values of the overdue debt indicator, which show the emergence of negative trends in the banking sector, the imputed overdue debt for each bank is determined at which the capital adequacy ratio of the corresponding bank will stand at 10%[83].

Subsequently, to ***monitor the risk of lending to non-financial corporations,*** banks are grouped in ascending order of the imputed overdue debt, i.e. by the reduction of the risk of the capital adequacy ratio falling to the threshold level of 10%. A group of banks (risk group) with the lowest imputed overdue debt levels (maximum risk) is selected. They account for 5% of aggregate banking sector assets. The presumption is that a banking sector in which “risk group” banks account for such a large part of aggregate assets is likely to have systemic problems. The highest level of imputed overdue debt in this group of banks is regarded as the threshold level and tentative lower limit of the yellow zone (green/yellow zone).

Credit institutions are selected to determine the lower limit of the red zone (yellow/red zone) in the same manner. These account for 10% of aggregate banking sector assets. Such a large share of problem banks in aggregate banking sector assets is assumed to increase the likelihood of a systemic banking crisis significantly. The highest imputed overdue debt level in this group of banks is considered to be the tentative lower limit of the red zone.

The limits of the zones are common for the banking sector as a whole and the individual groups of banks.

The share of loans extended to borrowers in financially troubled industries in each region[84] is an additional factor of high credit risk concentration.

[82] The reports of the 200 largest banks by assets, excluding Sberbank and Vneshtorgbank, are analysed as the risk of consumer lending and liquidity are monitored.

[83] Bank of Russia Instruction of January 16, 2004, No.110-I “On Banks' Prudential Ratios”, sets the minimum N1 ratio depending on the size of a bank's own funds (capital):

— 10% for the banks with own funds (capital) of no less than 5 million euros;

— 11% for the banks with own funds (capital) of less than 5 million euros.

[84] These industries are determined on the basis of data resulting from the Bank of Russia monitoring of the financial condition of non-financial corporations.

Monitoring is conducted on a quarterly basis.

To ***monitor the risk of lending to households,*** the Bank of Russia determines the threshold levels (zoning) of overdue household loans in total portfolio of these loans, taking into account the calculation of the adjusted capital adequacy ratio.

The imputed overdue debt on loans to households in total loans to them, when at least one of the 30 largest banks by assets has the adjusted capital adequacy ratio of 10%, is regarded as a benchmark when determining the lower limit of the red zone. Any excess over the red zone limit has the potential to provoke a systemic banking crisis, assuming that financial instability and/or withdrawal from the market of just one large retail bank may cause panic among the population and trigger a crisis.

The ratio of overdue household loans to capital is an additional indicator of the risk involved in lending to individuals.

To evaluate the economic implications of the scale of lending to households and related risks, the Bank of Russia regularly verifies the results of monitoring, taking into account the dynamics of the ratio of household loans to GDP and to household income.

Monitoring is conducted on a quarterly basis.

Liquidity monitoring subsystem

Liquidity monitoring is based on an analysis of the following major indicators:

— the share of balances in bank correspondent and deposit accounts with the Bank of Russia and correspondent accounts with credit institutions in aggregate banking sector assets;
— the instant liquidity ratio;
— the current liquidity ratio.

Threshold levels for each indicator in each group of banks were determined on the basis of the retrospective analysis of indicators between October 1, 2004 and October 1, 2005.

The upper limit of the yellow zone is determined as the average ratio minus one standard deviation and the red zone as the average ratio minus three standard deviations. The values obtained in this manner were adjusted by the results of a retrospective analysis of the liquidity ratios of the banks stripped of their licences.

The monitoring reveals the banks in the red zone on the basis of at least two of the ratios described above.

The following two factors are also taken into account when analysing:

— deviation of the current value of each of the three indicators from the highest value registered in the past three months;
— payment documents that were unmet within the reporting month (according to data collected by the Moscow Region settlement system).

Monitoring is conducted on a monthly basis.

***

The Bank of Russia is currently testing the methodologies described above and upgrading the monitoring techniques.

IV.2. Bank of Russia Participation in IMF Coordinated Compilation Exercise for Financial Soundness Indicators (FSIs)

The Bank of Russia is participating in the IMF Coordinated Compilation Exercise (CCE) for Financial Soundness Indicators (FSIs), which is a phase of the IMF Work Program aiming to strengthen macroprudential surveillance of the IMF member countries' financial systems. The analysis of the FSIs for the banking sector was a component of the Financial Sector Assessment Programme (FSAP) for Russia, implemented by the Bank of Russia in collaboration with the IMF and World Bank in 2001—2003.

Using the experience from FSAPs and the results of the 2000 survey of the current FSI calculation and analysis practices of more than 120 participating countries, the IMF developed the Compilation Guide on Financial Soundness Indicators. FSIs represent a set of indicators on the current financial health and soundness of the financial institutions in a country, including non-bank financial institutions, and their corporate and household counterparts, real estate market and financial market liquidity.

As envisaged in the Terms of Reference of the CCE in 2005 the Bank of Russia prepared and agreed with the IMF the drafts of FSI metadata adapted to the peculiarities of Russia's financial market and its regulation, and accounting and reporting practices.

In April 2005, the Bank of Russia compiled and sent to the IMF the first draft of FSI metadata for the banking sector and financial market (government securities market) as an interim result of the CCE. In December 2005, the second draft of FSI metadata, including FSIs for the real estate market, was sent to the IMF.

FSI coordinators and compilers held a regional meeting in Vienna during May 9-13, 2005, to discuss common and country-specific, including Russia-specific, problems involved in compiling metadata.

The FSIs compiled by the Bank of Russia for the CCE include:

1. All 12 core FSIs, which pertain to the banking sector only, and nine out of the 13 encouraged FSIs for the banking sector.

Bank of Russia-calculated FSIs

TABLE 4.1

	Financial Soundness Indicator
Core Set	
Banking sector	
Capital adequacy	Regulatory capital to risk-weighted assets Regulatory Tier 1 capital to risk-weighted assets
Asset quality	Non-performing loans net of provisions to capital Non-performing loans to total gross loans Sectoral distribution of loans to total loans
Earnings and profitability	Return on assets Return on equity Interest margin to gross income Non-interest expenses to gross income
Liquidity	Liquid assets to total assets (liquid asset ratio) Liquid assets to short-term liabilities
Sensitivity to market risk	Net open position in foreign exchange to capital
Encouraged Set	
Banking sector	Capital to assets Large exposures to capital Geographical distribution of loans to total loans Trading income to total income Personnel expenses to non-interest expenses Spread between reference lending and deposit rates Customer deposits to total (non-interbank) loans Foreign-currency-denominated loans to total loans Foreign-currency-denominated liabilities to total liabilities
Market liquidity	Average bid-ask spread in the government securities market Average daily turnover ratio in the government securities market
Real estate markets	Loans extended to construction companies to total loans Residential real estate loans to total loans

2. Two indicators characterising financial market (government securities market) liquidity and two out of the three encouraged FSIs for the real estate market.

When compiling FSIs, the Bank of Russia tries to follow the methodologies recommended by the Compilation Guide as closely as possible. However, there are some differences in Russia and other countries arising from differences in legislation and regulation, and national accounting and reporting practices. The Bank of Russia, for example, includes all credit institutions in the FSIs calculation, not only deposit-takers, and Russian credit institutions do not account for derivatives on their balance sheets.

Indicators similar to FSIs are widely used by the Bank of Russia in compiling the monthly *Russian Banking Sector Review* and the annual *Banking Supervision Report.* In addition, the methodologies recommended by the Compilation Guide were taken into account when developing the banking sector stability monitoring system. However, the Bank of Russia often uses more stringent standards in respect to the evaluation of non-performing loans or short-term assets and liabilities.

The Bank of Russia will continue to participate in the CCE in 2006.The final draft of metadata and data on FSIs will be placed on the IMF web site.

The Bank of Russia intends to continue to upgrade the FSI calculation methodology, especially in connection with the Russian banking sector’s conversion to the IFRS. It also plans to enlarge the set of FSIs by enlisting other agencies to the Exercise.

IV.3. Banking sector clustering

For the purposes of in-depth analysis in compiling the *Banking Supervision Report,* the Bank of Russia clusters the banking sector into several groups of banks with similar characteristics, such as ownership structure, business models and size, which allows it to identify the trends, factors and causes of processes undetectable by analysing averages. The banking sector's clustering has several stages.

At the first stage the institutions classified into separate groups are as follows:

— *non-bank credit institutions;*

— banks in which more than 50% of authorised capital is owned *by the state* (executive authorities and federal and regional government-controlled unitary enterprises and enterprises controlled by the Russian Federal Property Fund), the Bank of Russia and banks that are members of the banking groups formed by these banks[85];

— banks with a 50%-plus stake owned *by non-residents.*

At the second stage banks from among the 200 largest banks by assets are analysed. Of these, the banks which have not been included in any of the three groups indicated above, are divided on the basis of professional judgement into the banks controlled by one owner or a group of related owners ("intra-group" banks) and other large banks ("diversified" banks). Professional judgement is formed on the basis of several criteria. Among the relationship criteria are the existence of one owner or a group of related owners with a 50%-plus stake in authorised capital, a persistently high ratio of large credit claims per borrower and the signs of preferential lending to borrowers related with a creditor bank[86]. Banks with these signs are classified as "intra-group" banks. The list of "intra-group" banks also comprises banks, including banks that are not in the top 200, which are members of the banking groups led by the "intra-group" banks indicated above. The other banks from the top 200 that are not classified as "intra-group" are included in the group of "diversified" banks.

All other banks not included in any of the five groups indicated above are considered at the third stage. These are *medium-sized and small banks,* which are divided into two groups by location: the medium-sized and small banks based in Moscow and the Moscow Region and regional medium-sized and small banks.

Hence, there are seven groups of credit institutions:

1. State-controlled banks;
2. Banks controlled by foreign capital;
3. "Intra-group" banks;
4. "Diversified" banks;
5. Medium-sized and small banks based in Moscow and the Moscow Region;
6. Regional medium-sized and small banks;
7. Non-bank credit institutions.

[85] On the basis of Reporting Form 0409801 "Statement on the Makeup of a Consolidated Banking Group".

[86] The source of data for the establishment of these criteria is credit institutions' reporting and results of inspections, especially those conducted while selecting banks to the deposit insurance system.

IV.4. Statistical Appendix

Dynamics of key macroeconomic indicators in 2002—2005

TABLE 1

Indicator	2002	2003	2004	2005
GDP (in market prices), billion rubles	10,830.5	13,243,2	16,966.4	21,598.0
as % of previous year	104.7	107.3	107.2	106.4
Federal budget surplus, as % of GDP	1.4	1.7	4.3	7.5
Industrial output, as % of previous year	103.1	108.9	108.3	104.0
Agricultural output, as % of previous year	101.5	101.4	103.1	102.0
Retail trade turnover, as % of previous year	109.3	108.8	113.3	112.8
Fixed capital investment, as % of previous year	102.8	112.5	111.7	110.7
Household real disposable income, as % of previous year	111.1	115.0	110.4	109.3
Unemployment rate, as % of economically active population (average for period)	8.1	8.6	8.2	7.6
Consumer price index (December as % of December of previous year)	115.1	112.0	111.7	110.9
Ruble/US dollar nominal rate for period	31.35	30.68	28.81	28.28*

** Estimate.*

Macroeconomic indicators of the Russian banking sector

TABLE 2

Indicator	1.01.02	1.01.03	1.01.04	1.01.05	1.01.06
Banking sector assets (liabilities), billion rubles	3,159.7	4,145.3	5,600.7	7,136.9	9,750.3
as % of GDP	35.3	38.3	42.3	42.1	45.1
Banking sector own funds (capital), billion rubles	453.9	581.3	814.9	946.6	1,241.8
as % of GDP	5.1	5.4	6.2	5.6	5.7
as % of banking sector assets	14.4	14.0	14.6	13.3	12.7
Loans and other funds extended to non-financial corporations and individuals, including overdue debt, billion rubles	1,323.6	1,796.2	2,684.7	3,887.6	5,454.0
as % of GDP	14.8	16.6	20.3	22.9	25.3
as % of banking sector assets	41.9	43.3	47.9	54.5	55.9
Securities acquired by banks, billion rubles	562.0	779.9	1,002.2	1,086.9	1,539.4
as % of GDP	6.3	7.2	7.6	6.4	7.1
as % of banking sector assets	17.8	18.8	17.9	15.2	15.8
Household deposits, billion rubles	678.0	1,029.7	1,517.8	1,977.2	2,754.6
as % of GDP	7.6	9.5	11.5	11.7	12.8
as % of banking sector liabilities	21.5	24.8	27.1	27.7	28.3
as % of household money income	12.7	15.1	17.1	18.1	20.5
Funds attracted from enterprises and organisations*, billion rubles	902.6	1,091.4	1,384.8	1,986.1	2,953.1
as % of GDP	10.1	10.1	10.5	11.7	13.7
as % of banking sector liabilities	28.6	26.3	24.7	27.8	30.3

** Including deposits, government extra-budgetary funds, funds of the Finance Ministry, financial authorities, customers in factoring and forfeiting operations, float, and funds written down from customers' accounts but not entered in a credit institution's correspondent account.*

Quantitative characteristics of Russian credit institutions

TABLE 3

Indicator	1.01.05	1.04.05	1.07.05	1.10.05	1.01.06
Credit institutions registered by the Bank of Russia and other authorities	1,518	1,487	1,460	1,424	1,409
Operating credit institutions (credit institutions licensed to conduct banking operations)	1,299	1,289	1,281	1,263	1,253
Credit institutions which have been registered by the Bank of Russia but have not yet paid up their authorized capital and have not received a banking licence (within the time period set by legislation)	1	2	1	1	2
Credit institutions which had their banking licence revoked (cancelled)	218	196	178	160	154
Credit institutions licensed to conduct operations in foreign currency	839	833	830	826	827
Credit institutions with general licences	311	313	310	304	301

Data on the registration and licensing of credit institutions as of January 1, 2006*

TABLE 4

Registration of credit institutions	
1. Credit institutions[1] registered by the Bank of Russia or by the Registration Authority on the basis of the Bank of Russia decision, total[2]	1,409
of which:	
— banks	1,356
— non-bank credit institutions	53
1.1. Registered wholly foreign-owned credit institutions	42
1.2. Credit institutions which have been registered by the Bank of Russia but have not yet paid up authorised capital and have not received a banking licence (within the time period set by legislation)	2
of which:	
— banks	2
— non-bank credit institutions	0
2. Non-bank credit institutions registered by other authorities before July 1, 2002	0
Operating credit instituions	
3. Credit institutions licensed to conduct banking operations, total[3]	1,253
of which:	
— banks	1,205
— non-bank credit institutions	48
3.1. Credit institutions with licences (permits):	
— to take household deposits	1,045
— to conduct operations in foreign currency	827
— general licences	301
— to conduct operations with precious metals	
— permits	4
— licences[4]	180
3.2. Credit institutions with foreign stakes in authorised capital, total	136
of which:	
— wholly foreign-owned credit institutions	41
— credit institutions with a 50%-plus foreign stake	11
3.3. Credit institutions registered as participants in the deposit insurance system	930
4. Registered authorised capital of operating credit institutions, million rubles	444,377
5. Branches of operating credit institutions in Russia, total	3,295
of which:	
— Sberbank branches[5]	1,009
— branches of wholly foreign-owned credit institutions	29
6. Branches of operating credit institutions abroad, total[6]	3
7. Non-resident bank branches in Russia	0

END

8. Representative offices of operating Russian credit institutions, total[7]	467
of which:	
— in Russia	422
— in non-CIS countries	31
— in CIS countries	14
Licence revocation and liquidation of legal entities	
9. Credit institutions which had their banking licence revoked (cancelled) but were not struck off the State Register of Credit Institutions[8]	154
10. Liquidated credit institutions struck off the State Register of Credit Institutions, total[9]	1,687
of which:	
— due to licence revocation (cancellation)	1,305
— due to reorganisation	381
of which:	
— by merger	0
— by acquisition	381
of which:	
— transformed into other banks' branches	337
— merged with other banks (without establishing a branch)	44
— due to non-compliance with authorised capital payment requirements set by legislation	1

** Including data provided by the Registration Authority as of the reporting date.*

[1] The term "credit institution" in this Table denotes one of the following:
— a legal entity registered by the Bank of Russia (prior to July 1, 2002) or the Registration Authority and having the right to conduct banking operations;
— a legal entity registered by the Bank of Russia (prior to July 1, 2002), or the Registration Authority, which had but lost the right to conduct banking operations;
— a legal entity registered by other authorities (before the Federal Law "On Banks and Banking Activities" came into force) and having a Bank of Russia licence to conduct banking operations.

[2] Credit institutions which have the status of a legal entity as of the reporting date, including credit institutions that have lost the right to conduct banking operations but have not yet been liquidated as legal entities.

[3] Credit institutions registered by the Bank of Russia (prior to July 1, 2002) or the Registration Authority and having the right to conduct banking operations and also non-bank credit institutions registered by other authorities and licensed by the Bank of Russia to conduct banking operations.

[4] Issued since December 1996 in accordance with Bank of Russia Letter of December 3, 1996, No. 367.

[5] Sberbank branches put on the State Register of Credit Institutions and assigned serial numbers.

[6] Branches opened by Russian credit institutions abroad.

[7] Representative offices of Russian credit institutions abroad include the offices of whose opening abroad the Bank of Russia has been notified.

[8] Total number of credit institutions stripped of a banking licence by the Bank of Russia, including credit institutions struck off the State Register of Credit Institutions, stands at 1,469.

[9] Since July 1, 2002, a liquidated credit institution is struck off the State Register of Credit Institutions as a legal entity only after its liquidation has been registered by the Registration Authority.

Dynamics of operating credit institutions by organisational and legal form structure

TABLE 5

Title	1.01.05		1.01.06	
	Number	% share	Number	% share
Operating credit institutions with a licence to conduct banking operations, total	**1,299**	**100**	**1,253**	**100**
of which:				
— joint-stock companies	824	63.43	799	63.7
— close-end joint-stock companies	341	26.25	330	26.34
— open-end joint-stock companies	483	37.18	469	37.43
— unit trusts	474	36.49	454	36.23
— additional liability companies	1	0.08	—	—
— limited liability companies	473	36.41	454	36.23
— Russian Finance Corporation (government enterprise)	1	0.08	—	—

Number of credit institutions and their branches by region as of January 1, 2006

TABLE 6

Region	No. of credit institutions in region	No. of branches in region		
		Total	Credit institutions with head office in this region	Credit institutions with head office in another region
1	2	3	4	5
Total in Russia:	**1,253**	**3,295**	**828**	**2,467**
Central Federal District	**714**	**728**	**218**	**510**
Belgorod Region	6	35	5	30
Bryansk Region	1	26	2	24
Vladimir Region	3	26	0	26
Voronezh Region	4	43	1	42
Ivanovo Region	5	21	3	18
Kaluga Region	5	28	2	26
Kostroma Region	5	15	1	14
Kursk Region	2	21	0	21
Lipetsk Region	2	20	1	19
Orel Region	2	22	3	19
Ryazan Region	4	24	1	23
Smolensk Region	4	30	5	25
Tambov Region	2	21	7	14
Tver Region	7	38	3	35
Tula Region	6	30	2	28
Yaroslavl Region	10	36	4	32
Moscow	631	143	37	106
Moscow Region	15	149	9	140
Moscow and Moscow Region (for the record)	646	292	178	114
North-Western Federal District	**84**	**376**	**55**	**321**
Republic of Karelia	1	20	2	18
Komi Republic	4	36	7	29
Arkhangelsk Region	4	32	0	32
of which: Nenets Autonomous Area	0	2	0	2
Vologda Region	8	29	9	20
Kaliningrad Region	12	31	6	25
Leningrad Region	3	42	2	40
Murmansk Region	4	29	2	27
Novgorod Region	2	16	2	14
Pskov Region	4	11	0	11
St Petersburg	42	130	25	105
Southern Federal District	**128**	**471**	**150**	**321**
Republic of Adygeya	5	6	1	5
Republic of Daghestan	36	75	63	12
Republic of Ingushetia	2	5	1	4
Kabardino-Balkar Republic	6	11	3	8
Republic of Kalmykia — Khalmg Tangch	2	4	0	4
Karachai-Cherkess Republic	5	5	0	5
Republic of North Ossetia — Alania	6	18	8	10
Chechen Republic	0	1	0	1
Krasnodar Territory	21	106	22	84
Stavropol Territory	10	53	8	45
Astrakhan Region	5	29	7	22
Volgograd Region	6	63	12	51
Rostov Region	24	95	25	70

END

Region	No. of credit institutions in region	No. of branches in region		
		Total	Credit institutions with head office in this region	Credit institutions with head office in another region
1	2	3	4	5
Volga Federal District	**146**	**671**	**152**	**519**
Republic of Bashkortostan	12	49	0	49
Republic of Marii El	1	25	4	21
Republic of Mordovia	4	18	6	12
Republic of Tatarstan	27	103	56	47
Udmurt Republic	9	29	0	29
Chuvash Republic	5	21	0	21
Kirov Region	3	27	0	27
Nizhny Novgorod Region	19	86	33	53
Orenburg Region	9	48	4	44
Penza Region	2	32	0	32
Perm Region	9	56	3	53
Samara Region	23	82	22	60
Saratov Region	17	66	21	45
Ulyanovsk Region	6	29	3	26
Ural Federal District	**67**	**381**	**143**	**238**
Kurgan Region	5	27	0	27
Sverdlovsk Region	27	89	21	68
Tyumen Region	23	157	80	77
of which: Khanty-Mansi Autonomous Area	12	56	14	42
Yamalo-Nenets Autonomous Area	5	36	14	22
Chelyabinsk Region	12	108	42	66
Siberian Federal District	**71**	**452**	**53**	**399**
Republic of Altai	5	3	1	2
Republic of Buryatiya	2	28	3	25
Republic of Tyva	2	4	0	4
Republic of Khakassia	3	12	1	11
Altai Territory	8	58	13	45
Krasnoyarsk Territory	6	80	10	70
of which: Taimyr Autonomous Area	0	1	0	1
Evenk Autonomous Area	0	0	0	0
Irkutsk Region	9	64	11	53
of which: Ust-Orda Buryat Autonomous Area	0	3	0	3
Kemerovo Region	8	38	0	38
Novosibirsk Region	14	51	1	50
Omsk Region	8	49	0	49
Tomsk Region	4	32	9	23
Chita Region	2	33	4	29
of which: Agin-Buryat Autonomous Area	0	3	0	3
Far Eastern Federal District	**43**	**216**	**57**	**159**
Republic of Sakha (Yakutia)	6	57	9	48
Primorskiy (Maritime) Territory	9	42	17	25
Khabarovsk Territory	6	25	5	20
Amur Region	5	19	4	15
Kamchatka Region	8	19	7	12
of which: Koryak Autonomous Area	1	2	0	2
Magadan Region	3	19	6	13
Sakhalin Region	6	22	9	13
Jewish Autonomous Region	0	6	0	6
Chukchee Autonomous Area	0	7	0	7

1. Columns 2 and 3 relating to St Petersburg and the Leningrad Region show the number of credit institutions and the number of branches entered into the State Register of Credit Institutions by the Bank of Russia St Petersburg Branch and Main Division for the Leningrad Region respectively.

2. Columns 4 and 5 relating to the Moscow Region show the number of branches whose parent credit institution is located in this region (in Moscow and the Moscow Region) and in other regions.

Provision of Russian regions with banking services as of January 1, 2006*

TABLE 7

Region	No. of credit institutions	No. of branches and additional offices	Assets (net), million rubles	Loans and other placements with resident non-financial corporations and individuals, million rubles	Household deposits, million rubles	Gross Regional Product in 2005, billion rubles (estimate)	Population, thousand (estimate)	Average monthly per capita money income in 2005, rubles	Institutional saturation with banking services (by population)	Financial saturation with banking services (by assets)	Financial saturation with banking services (by lending volume)	Savings index (per capita deposits to income)	Composite index of region's provision with banking services
1	2	3	4	5	6	7	8	9	10	11	12	13	14
Central Federal District (excluding Moscow and Moscow Region)	**68**	**1,534**	**424,308**	**334,503**	**234,719**	**1,629**	**20,302**	**4,951**	**0.80**	**1.00**	**1.19**	**1.14**	**1.02**
Belgorod Region	6	113	45,960	39,687	20,725	144	1,511	5,279	0.80	1,23	1.59	1.27	1.19
Bryansk Region	1	75	17,096	13,561	10,626	70	1,331	4,742	0.58	0.94	1.12	0.82	0.84
Vladimir Region	3	105	26,381	20,703	17,739	95	1,472	4,000	0.75	1.07	1.26	1.47	1.10
Voronezh Region	4	126	56,758	43,975	31,374	149	2,313	5,039	0.57	1.47	1.70	1.32	1.17
Ivanovo Region	5	77	15,724	8,045	10,054	55	1,100	3,281	0.76	1.10	0.84	1.36	0.99
Kaluga Region	5	95	21,147	14,380	12,989	83	1,014	5,333	1,00	0.99	1.01	1.17	1.04
Kostroma Region	5	62	10,867	7,658	6,970	49	708	4,657	0.96	0.86	0.91	1.03	0.94
Kursk Region	2	112	34,525	30,891	11,290	106	1,184	5,113	0.98	1.26	1.69	0.91	1.17
Lipetsk Region	2	77	31,995	25,632	13,778	183	1,181	5,511	0.68	0.67	0.81	1.03	0.79
Orel Region	2	71	12,714	10,947	7,812	66	834	4,668	0.89	0.74	0.96	0.98	0.89
Ryazan Region	4	86	23,159	18,530	14,033	102	1,182	4,641	0.77	0.88	1.05	1.25	0.97
Smolensk Region	4	76	20,869	17,921	11,176	73	1,006	5,364	0.81	1.10	1.42	1.01	1.06
Tambov Region	2	89	16,866	14,582	9,204	77	1,131	5,144	0.82	0.85	1.10	0.77	0.88
Tver Region	7	95	19,768	13,928	12,407	112	1,406	5,448	0.74	0.68	0.72	0.79	0.73
Tula Region	6	166	32,454	25,872	19,806	112	1,600	4,816	1.09	1.11	1.33	1.26	1.20
Yaroslavl Region	10	109	38.024	28.190	24.737	154	1,328	5,907	0.91	0.95	1.05	1.54	1.09
North-Western Federal District	**84**	**1,792**	**744,532**	**397,016**	**307,961**	**1,879**	**13,628**	**8,381**	**1.40**	**1.53**	**1.22**	**1.32**	**1.36**
Republic of Karelia	1	79	13,198	11,012	7,810	71	698	6,720	1.17	0.71	0.89	0.81	0.88
Komi Republic	4	100	27,913	18,763	18,687	180	985	10,915	1.07	0.60	0.60	0.85	0.76
Arkhangelsk Region	4	111	27,188	21,750	16,476	196	1,292	7,584	0.91	0.53	0.64	0.82	0.71
Vologda Region	8	115	45,819	30,871	19,465	209	1,235	6,486	1.01	0.84	0.85	1.19	0.96
Kaliningrad Region	12	134	31,585	21,810	16,592	84	940	6,282	1.58	1.46	1.51	1.37	1.48
Leningrad Region	3	222	27,943	12,947	17,784	222	1,644	4,854	1.39	0.48	0.34	1.09	0.71
Murmansk Region	4	134	28,039	19,947	19,481	151	865	9,295	1.62	0.72	0.77	1.18	1.01
Novgorod Region	2	109	9,884	7,887	6,224	60	665	5,086	1.70	0.63	0.76	0.90	0.93
Pskov Region	4	81	8,876	5,349	5,714	47	725	4,852	1.19	0.73	0.66	0.79	0.82
St Petersburg	42	707	524,087	246,681	179,730	661	4,581	11,385	1.66	3.05	2.16	1.68	2.07

CONT.

1	2	3	4	5	6	7	8	9	10	11	12	13	14
Southern Federal District	**128**	**1,867**	**357,309**	**265,088**	**187,289**	**1,383**	**22,788**	**5,079**	**0.89**	**0.99**	**1.11**	**0.79**	**0.94**
Republic of Adygeya	5	36	3,275	2,329	2,257	17	443	3,759	0.94	0.74	0.79	0.66	0.78
Republic of Daghestan	36	135	9,128	4,453	2,560	97	2,641	4,725	0.66	0.36	0.27	0.10	0.28
Republic of Ingushetia	2	5	1,049	341	634	8	487	2,457	0.15	0.53	0.26	0.26	0.27
Kabardino-Balkar Republic	6	56	6,146	4,710	3,409	41	894	4,015	0.71	0.58	0.67	0.46	0.60
Republic of Kalmykia — Khalmg Tangch	2	30	2,256	1,900	744	14	289	2,333	1.13	0.60	0.76	0.54	0.73
Karachai-Cherkess Republic	5	36	3,637	2,866	1,421	18	432	4,188	0.97	0.76	0.90	0.38	0.71
Republic of North Ossetia — Alania	6	48	8,275	5,168	5,417	32	1,139	5,241	0.48	0.99	0.93	0.44	0.66
Krasnodar Territory	21	480	109,367	85,571	65,160	415	5,096	5,359	1.00	1.01	1.19	1.17	1.09
Stavropol Territory	10	410	47,979	36,440	27,651	169	2,708	5,119	1.58	1.09	1.24	0.97	1.20
Astrakhan Region	5	66	18,758	10,178	10,350	80	994	5,443	0.73	0.91	0.74	0.93	0.82
Volgograd Region	6	161	47,051	32,429	26,125	206	2,635	5,625	0.64	0.88	0.91	0.86	0.82
Rostov Region	24	403	98,827	78,313	41,087	285	4,303	6,262	1.01	1.33	1.59	0.74	1.12
Volga Federal District	**146**	**2,446**	**921,703**	**660,160**	**383,299**	**3,076**	**30,508**	**5,976**	**0.86**	**1.15**	**1.24**	**1.03**	**1.06**
Republic of Bashkortostan	12	387	112,102	66,093	41,168	429	4,064	6,490	1.00	1.01	0.89	0.76	0.91
Republic of Marii El	1	45	8,022	6,824	4,143	39	712	3,216	0.66	0.80	1.02	0.88	0.83
Republic of Mordovia	4	88	15,102	11,253	6,175	67	856	3,998	1.09	0.87	0.98	0.88	0.95
Republic of Tatarstan	27	344	198,970	118,929	57,628	523	3,760	6,997	1.00	1.46	1.31	1.07	1.20
Udmurt Republic	9	129	43,742	35,130	15,638	137	1,544	4,462	0.91	1.23	1.49	1.11	1.17
Chuvash Republic	5	73	19,801	17,063	9,930	79	1,292	3,963	0.61	0.97	1.25	0.95	0.92
Kirov Region	3	104	22,787	18,795	12,461	94	1,443	4,453	0.75	0.93	1.16	0.95	0.94
Nizhny Novgorod Region	19	292	114,980	90,415	54,970	337	3,411	5,969	0.93	1.31	1.55	1.32	1.26
Orenburg Region	9	152	48,887	37,783	20,585	224	2,138	4,932	0.77	0.84	0.97	0.95	0.88
Penza Region	2	82	19,249	14,447	12,383	80	1,408	4,103	0.61	0.93	1.05	1.05	0.89
Perm Region	9	241	84,281	70,399	38,414	341	2,748	7,803	0.93	0.95	1.19	0.88	0.98
Samara Region	23	261	159,564	120,816	68,589	445	3,188	9,057	0.91	1.38	1.57	1.16	1.23
Saratov Region	17	160	54,619	35,731	29,837	195	2,608	4,827	0.69	1.08	1.06	1.16	0.98
Ulyanovsk Region	6	88	19,597	16,484	11,378	87	1,336	4,426	0.72	0.87	1.10	0.94	0.90
Ural Federal District	**67**	**1,479**	**587,388**	**319,347**	**223,258**	**3,330**	**12,239**	**9,127**	**1.29**	**0.68**	**0.55**	**0.98**	**0.83**
Kurgan Region	5	75	10,016	8,045	5,324	57	979	4,520	0.83	0.67	0.81	0.59	0.72
Sverdlovsk Region	27	561	200,559	138,756	73,436	467	4,409	8,360	1.36	1.65	1.72	0.97	1.39
Tyumen Region	23	455	283,333	105,594	102,128	2,418	3,319	14,337	1.47	0.45	0.25	1.05	0.65
Chelyabinsk Region	12	388	93,480	66,951	42,369	388	3,531	6,463	1.15	0.93	1.00	0.91	0.99

END

1	2	3	4	5	6	7	8	9	10	11	12	13	14
Siberian Federal District	**71**	**1,824**	**485,803**	**376,296**	**211,004**	**2,158**	**19,676**	**6,525**	**0.98**	**0.87**	**1.01**	**0.80**	**0.91**
Republic of Altai	5	17	2,578	1,990	814	12	205	4,364	1.09	0.85	0.99	0.45	0.80
Republic of Buryatiya	2	126	16,554	12,104	5,967	83	963	5,765	1.35	0.77	0.85	0.52	0.83
Republic of Tyva	2	19	1,586	1,350	765	12	309	4,010	0.69	0.49	0.63	0.30	0.50
Republic of Khakassia	3	52	8,379	7,284	3,460	43	538	4,914	1.04	0.75	0.97	0.64	0.83
Altai Territory	8	227	53,906	42,107	18,975	142	2,543	4,472	0.94	1.46	1.71	0.82	1.18
Krasnoyarsk Territory	6	294	80,042	63,607	37,086	485	2,906	7,550	1.05	0.64	0.76	0.83	0.80
Irkutsk Region	9	253	54,481	43,459	29,181	267	2,527	7,030	1.05	0.79	0.94	0.80	0.89
Kemerovo Region	8	198	69,176	57,506	33,653	324	2,839	7,680	0.74	0.82	1.02	0.75	0.83
Novosibirsk Region	14	277	101,037	68,793	35,790	255	2,649	6,234	1.12	1.53	1.56	1.06	1.30
Omsk Region	8	139	54,338	43,408	22,788	266	2,035	6,922	0.74	0.79	0.94	0.79	0.81
Tomsk Region	4	111	30,511	24,725	14,880	187	1,035	7,935	1.13	0.63	0.76	0.89	0.83
Chita Region	2	111	13,215	9,965	7,645	81	1,129	5,653	1,02	0.63	0.71	0.59	0.72
Far Eastern Federal District	**43**	**805**	**199,834**	**127,735**	**108,310**	**873**	**6,547**	**8,545**	**1.32**	**0.88**	**0.85**	**0.95**	**0.98**
Republic of Sakha (Yakutia)	6	99	26,523	16,756	14,434	209	950	10,750	1.12	0.49	0.46	0.69	0.65
Primorskiy (Maritime) Territory	9	233	48,175	33,802	27,290	188	2,020	7,007	1.22	0.99	1.04	0.94	1.04
Khabarovsk Territory	6	167	56,725	37,836	29,673	172	1,412	9,070	1.25	1.27	1.27	1.13	1.23
Amur Region	5	110	18,350	14,243	7,735	84	881	6,084	1.33	0.84	0.98	0.71	0.94
Kamchatka Region	8	66	12,981	7,573	8,208	42	349	9,614	2.16	1.18	1.03	1.19	1.33
Magadan Region	3	39	10.975	5,990	5,093	30	172	10,783	2.49	1.40	1.15	1.34	1.52
Sakhalin Region	6	61	21,090	8,794	12,560	113	526	12,137	1.30	0.72	0.45	0.96	0.80
Jewish Autonomous Region	0	13	1,915	1,445	1,369	15	187	6,226	0.71	0.50	0.57	0.58	0.58
Chukchee Autonomous Area	0	17	3,100	1,298	1,947	19	51	12,997	3.40	0.62	0.39	1.44	1.04
Total (excluding Moscow and Moscow Region)	**607**	**11,747**	**3,720,876**	**2,480,146**	**1,655,839**	**14,327**	**125,687**	**6,435**	**1.00**	**1.00**	**1.00**	**1.00**	**1.00**

** Calculated in accordance with methodology developed by the Banking Regulation and Supervision Department of the Bank of Russia.*

Some performance indicators on credit institutions with foreign interest relative to indicators on operating credit institutions (%)

TABLE 8

	1.01.02	1.01.03	1.01.04	1.01.05	1.01.06
Credit institutions with a 50%-plus foreign stake					
Assets	8.8	8.1	7.4	7.6	8.3
Own funds (capital)	7.7	7.1	6.6	7.8	9.3
Correspondent accounts with non-resident banks	20.0	22.9	19.7	14.0	10.5
Loans and other placements with non-financial corporations, including non-resident legal entities	7.2	7.1	6.1	6.2	7.4
Loans, deposits and other placements with banks	31.3	25.9	22.0	15.8	17.1
Funds in household accounts	2.2	2.3	2.3	3.0	3.4
of which: household deposits	2.3	2.3	2.2	2.8	3.4
Funds attracted from enterprises and organisations*	11.7	10.4	9.3	9.4	9.6
of which: wholly foreign owned credit institutions					
Assets	5.2	5.6	5.6	5.9	8.0
Own funds (capital)	5.2	5.4	5.4	6.3	9.0
Correspondent accounts with non-resident banks	10.5	19.2	16.8	7.7	9.9
Loans and other funds placed with non-financial corporations, including non-resident legal entities	5.2	5.5	4.6	4.6	7.3
Loans, deposits and other placements with banks	20.4	16.3	17.0	11.4	16.8
Funds in household accounts	1.4	1.5	1.5	2.4	3.3
of which: household deposits	1.5	1.5	1.5	2.4	3.3
Funds attracted from enterprises and organisations*	5.3	5.5	5.7	6.6	9.4

** These include deposits, government extra-budgetary funds, funds of the Finance Ministry, financial authorities, customers in factoring and forfeiting operations, float, and funds written down from customers' accounts but not entered in a credit institution's correspondent account.*

Credit institutions' assets grouped by kind of investment (billion rubles)

TABLE 9

	Assets	1.01.05	1.04.05	1.07.05	1.10.05	1.01.06
1	Money, precious metals and gemstones, total	196.3	157.9	164.0	188.0	263.4
1.1	of which: money	190.7	153.7	159.2	176.5	255.2
2	Accounts with the Bank of Russia, total	695.5	607.4	453.6	595.6	684.1
	of which:					
2.1	Credit institutions' correspondent accounts with the Bank of Russia	463.3	301.6	259.5	353.2	487.5
2.2	Credit institutions' required reserves transferred to the Bank of Russia	121.6	133.2	137.2	149.9	161.3
2.3	Deposits placed with the Bank of Russia	91.4	149.8	34.4	64.4	7.2
3.	Correspondent accounts with credit institutions, total	227.8	225.4	270.0	318.3	257.5
	of which:					
3.1	Correspondent accounts with correspondent credit institutions (residents)	86.5	99.4	99.9	148.2	88.5
3.2	Correspondent accounts with non-resident banks	141.3	126.0	170.1	170.2	169.0
4	Securities acquired by banks, total	1,086.9	1,231.9	1,358.8	1,460.6	1,539.4
	of which:					
4.1	Debt obligations	752.6	857.6	937.1	1,011.3	1,036.6
	of which:					
4.1.1	Russian government debt obligations	435.6	476.5	475.1	492.4	492.0
4.2	Stocks and shares	140.9	156.0	185.0	213.1	292.8
	of which:					
4.2.1	Controlling shareholdings	19.6	20.1	20.6	21.0	64.9
4.3	Discounted promissory notes	193.4	218.3	236.6	236.3	210.1
5	Other shareholdings in authorised capital	6.1	7.3	9.1	8.8	10.7
6	Loan debt, total	4,463.8	4,845.7	5,399.4	5,769.3	6,371.1
	of which:					
6.1	Loans, deposits and other placements,	4,462.4	4,844.3	5,397.9	5,767.7	6,369.5
	including overdue debt	61.9	69.2	72.9	78.5	76.4
	of which:					
6.1.1	Loans and other placements with non-financial organisations	3,268.7	3,406.9	3,684.1	3,905.6	4,274.8
	of which overdue debt	49.5	53.8	53.8	55.7	53.8
6.1.2	Loans, deposits and other placements with banks	425.8	593.8	725.9	685.9	668.0
	of which overdue debt	3.3	3.3	3.2	3.1	0.2
6.2	Financing of government programmes and capital investment on a repayable basis	1.4	1.5	1.5	1.6	1.6
7	Fixed and intangible assets and inventories	222.8	235.6	245.1	259.4	283.4
8	Disposition of profits	34.4	42.5	28.0	45.9	61.2
9	Other assets, total	203.2	237.1	265.6	284.1	279.5
	of which:					
9.1	Float	80.9	104.0	124.3	123.2	116.8
9.2	Debtors	27.4	30.3	32.6	37.2	38.3
9.3	Overdue interest on loans	3.1	2.5	2.5	2.3	0.7
9.4	Deferred expenses	81.4	88.2	93.3	106.0	107.7
Total assets		**7,136.9**	**7,590.7**	**8,193.0**	**8,930.0**	**9,750.3**

Structure of credit institutions' liabilities by source of funds (billion rubles)

TABLE 10

	Liabilities	1.01.05	1.04.05	1.07.05	1.10.05	1.01.06
1	Bank funds and profits, total	1,006.1	1,058.1	1,092.8	1,196.3	1,320.2
	of which:					
1.1	Bank funds	806.7	813.5	912.7	946.1	1,015.6
1.2	Profits (losses), including financial results of previous years	199.4	244.6	180.0	250.2	304.5
	of which:					
1.2.1	Reporting year's profits (losses)	177.9	53.4	116.1	207.6	262.1
2	Loans, deposits and other funds received by credit institutions from the Bank of Russia	19.5	19.5	21.7	20.0	20.2
3	Bank accounts, total	116.3	128.8	134.3	182.9	126.6
	of which:					
3.1	Correspondent credit institutions' correspondent accounts (residents)	69.1	85.4	89.4	129.4	71.7
3.2	Non-resident banks' correspondent accounts	17.5	12.9	18.2	15.1	14.7
4	Loans, deposits and other funds received from other banks, total	737.1	783.9	866.0	913.0	1,086.4
	of which:					
4.1	Overdue debt	0.0	0.0	0.0	0.0	0.0
5	Customers' funds, total	4,151.5	4,456.2	4,891.5	5,341.4	5,818.9
	of which:					
5.1	Budget funds in settlement and current accounts	138.7	138.5	147.6	129.1	48.6
5.2	Government extra-budgetary funds in settlement and current accounts	19.2	24.1	27.9	30.1	17.9
5.3	Corporate funds in settlement, current and other accounts	1,273.1	1,316.4	1,429.5	1,522.6	1,674.1
5.4	Customer float	30.3	66.8	73.4	83.7	35.6
5.5	Organisations' deposits	564.0	615.1	688.8	820.3	936.4
5.6	Funds in household accounts	2,026.7	2,167.7	2,356.8	2,519.1	2,817.1
	of which:					
5.6.1	Household deposits	1,977.2	2,118.5	2,302.4	2,460.2	2.754.6
5.7	Other borrowed funds	94.7	122.4	161.6	230.0	280.0
5.8	Customers' funds in factoring and forfeiting operations	4.8	5.2	5.9	6.5	8.2
5.9	Funds written down from customers' accounts but not entered in a credit institution's correspondent account	0.1	0.1	0.1	0.1	0.9
6	Debt obligations issued, total	644.2	623.6	636.5	683.3	749.2
	of which:					
6.1	Bonds	30.6	33.2	37.2	45.9	67.3
6.2	Certificates of deposit	99.2	72.3	59.7	53.9	54.8
6.3	Savings certificates	3.6	4.3	5.2	5.7	6.6
6.4	Promissory notes and bank acceptances	506.2	508.9	529.1	572.4	614.5
7	Other liabilities, total	462.1	520.6	550.8	593.2	628.9
	of which:					
7.1	Provisions	257.9	268.1	281.5	307.4	343.0
7.2	Float	139.1	169.5	174.9	189.2	189.6
7.3	Creditors	7.5	16.4	21.1	12.8	10.3
7.4	Fixed and intangible asset depreciation	34.9	38.6	42.2	46.1	50.0
7.5	Deferred income	10.8	11.5	11.9	12.9	11.4
Total liabilities		**7,136.9**	**7,590.7**	**8,193.6**	**8,930.0**	**9,750.3**

Major characteristics of banking sector lending operations (billion rubles)

TABLE 11

	Indicators	Rubles					Foreign currency					Total				
		1.01.05	1.04.05	1.07.05	1.10.05	1.01.06	1.01.05	1.04.05	1.07.05	1.10.05	1.01.06	1.01.05	1.04.05	1.07.05	1.10.05	1.01.06
1.	Loans, deposits and other placements, total	3,125.9	3,302.6	3,608.4	3,963.4	4,362.6	1,336.5	1,541.7	1,789.5	1,804.3	2,006.9	4,462.4	4,844.3	5,397.9	5,767.7	6,369.5
	of which: overdue debt	47.3	54.0	57.2	60.1	64.6	14.6	15.2	15.7	18.3	11.8	61.9	69.2	72.9	78.5	76.4
1.1.	Loans and other placements with resident non-financial organisations	2,280.0	2,363.1	2,544.1	2,735.4	2,904.2	869.9	933.2	1,021.2	1,040.5	1,206.4	3,149.9	3,296.3	3,565.3	3,775.8	4,110.6
	of which: overdue debt	36.3	40.1	39.9	42.2	44.1	12.4	13.1	13.3	12.9	9.1	48.7	53.1	53.2	55.0	53.2
1.2.	Loans and other placements with non-resident legal entities, except banks	18.7	18.9	19.1	19.2	18.3	100.1	91.8	99.7	110.6	145.8	118.8	110.6	118.7	129.8	164.1
	of which: overdue debt	0.2	0.3	0.2	0.2	0.2	0.6	0.3	0.3	0.4	0.3	0.8	0.6	0.6	0.7	0.6
1.3.	Loans, deposits and other placements with financial sector	209.8	228.1	252.8	268.9	300.9	79.0	76.2	89.5	89.2	102.7	288.9	304.3	342.4	358.1	403.6
	Including: overdue debt	3.4	3.3	3.2	0.2	0.2	0.0	0.0	0.0	0.0	0.0	3.4	3.3	3.2	0.2	0.2
	of which:															
1.3.1.	Loans, deposits and other placements with resident credit institutions	162.9	187.7	200.0	205.2	230.9	66.9	65.7	76.9	73.5	85.4	229.8	253.4	276.9	278.6	316.3
	of which: overdue debt	3.3	3.3	3.1	0.2	0.2	0.0	0.0	0.0	0.0	0.0	3.3	3.3	3.1	0.2	0.2
1.3.2.	Loans, deposits and other placements with resident financial organisations of different forms of ownership	46.9	40.4	52.8	63.7	70.0	12.1	10.5	12.6	15.7	17.3	59.0	50.8	65.5	79.4	87.3
	of which: overdue debt	0.06	0.02	0.02	0.00	0.06	0.01	0.01	0.01	0.01	0.01	0.07	0.03	0.03	0.01	0.06
1.4.	Loans, deposits and other placements with non-resident banks	14.5	14.1	9.5	8.8	20.0	181.4	326.2	439.5	398.5	331.7	196.0	340.3	449.0	407.3	351.7
	of which: overdue debt	0.00	0.00	0.00	0.00	0.00	0.02	0.02	0.02	2.87	0.01	0.02	0.02	0.02	2.88	0.02
1.5.	Loans and other funds provided to government financial agencies and extra-budgetary funds	53.3	65.9	61.4	61.0	63.6	1.3	0.9	1.3	1.3	1.6	54.6	66.8	62.7	62.3	65.2
	of which: overdue debt	0.36	0.71	0.45	0.42	0.27	0.04	0.03	0.00	0.00	0.00	0.40	0.73	0.45	0.42	0.27
1.6.	Loans extended to resident individuals	525.2	566.7	676.3	826.3	1,000.8	91.3	99.6	124.1	144.5	174.1	616.5	666.3	800.4	970.8	1,174.9
	of which: overdue debt	7.0	9.5	13.4	17.1	19.7	1.3	1.6	1.8	1.9	2.1	8.4	11.1	15.2	19.0	21.8
1.7.	Loans extended to non-resident individuals	0.2	0.2	0.2	0.3	0.2	2.1	2.2	2.8	3.5	4.1	2.3	2.4	2.9	3.7	4.3
	of which: overdue debt	0.01	0.01	0.01	0.01	0.01	0.20	0.20	0.21	0.21	0.21	0.21	0.21	0.23	0.22	0.22
	For the record:															
	Overdue interest on loans, deposits and other placements with residents	1.4	1.2	1.0	0.8	0.7	1.7	1.3	1.5	1.5	0.0	3.1	2.5	2.5	2.3	0.7
	Overdue interest on loans, deposits and other placements with non-residents	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.01	0.00	0.00	0.00	0.00	0.01	0.00
	Residents promissory notes discounted by credit institutions	166.0	188.8	205.7	221.5	198.5	20.7	22.0	23.8	11.5	9.6	186.7	210.8	229.5	233.1	208.1
	Non-residents promissory notes discounted by credit institutions	0.5	0.5	0.5	0.0	0.0	6.1	7.0	6.7	3.2	2.0	6.6	7.5	7.2	3.2	2.0

Number of Bank of Russia inspections of credit institutions and their branches in 2005

TABLE 12

	No. of inspections conducted according to Summary Annual Plan			Unscheduled inspections			Total		
	comprehensive inspections	selective inspections	total	comprehensive inspections	selective inspections	total	comprehensive inspections	selective inspections	total
Moscow	80	145	225	5	328	333	85	473	558
Central Federal District	50	201	251	5	41	46	55	242	297
North-Western Federal District	57	92	149	0	21	21	57	113	170
Southern Federal District	88	190	278	0	62	62	88	252	340
Volga Federal District	70	172	242	2	56	58	72	228	300
Ural Federal District	18	140	158	1	24	25	19	164	183
Siberian Federal District	40	130	170	0	25	25	40	155	195
Far Eastern Federal District	36	64	100	0	20	20	36	84	120
In addition, inspections conducted by Bank of Russia Main Inspectorate for Credit Institutions	0	0	0	1	57	58	1	57	58
TOTAL	**439**	**1,134**	**1,573**	**14**	**634**	**648**	**453**	**1,768**	**2,221**

Quantitative and qualitative characteristics of the supervisory staff at the Bank of Russia head office and regional branches as of January 1, 2006

TABLE 13

Division title	Total number of positions as of January 1, 2006	Total number of employees as of January 1, 2006 (excluding part-timers)	of whom:							
			age			education		length of work in banking system		women
			under 30 (born in 1976 and later)	50 years and over (born in 1955 and earlier)	of whom: women aged 55 years and over and men aged 60 years and over	higher	secondary vocational	under 3 years	15 years and over	
Head office										
Banking Regulation and Supervision Department	182	173	25	64	20	168	5	14	53	124
Credit Institution Licensing and Financial Rehabilitation Department	142	136	26	26	11	130	5	17	30	102
Financial Monitoring and Foreign Exchange Control Department	110	98	24	23	8	95	1	12	8	57
Main Inspectorate for Credit Institutions	156	149	32	33	5	147	2	49	12	81
Head office total	**590**	**556**	**107**	**146**	**44**	**540**	**13**	**92**	**103**	**364**
Regional branches										
Credit Institution Supervision Division (Section)	1,262.5	1,242	168	233	73	1,190	47	67	449	1,550
Credit Institution Inspection Division (Section)	1,004	984	149	187	38	964	19	66	217	552
Financial Monitoring and Foreign Exchange Control Division (Section)	618	608	120	75	20	591	13	41	133	412
Credit Institution Licensing Division (Section)	296	292	44	50	14	282	7	18	82	246
Sections of the Moscow Branch	647	642	208	108	37	574	59	78	76	456
Main Regional Divisions/National Banks total	**3,827.5**	**3,768**	**689**	**653**	**182**	**3,601**	**145**	**270**	**957**	**2,716**
Bank of Russia total	**4,417.5**	**4,324**	**796**	**799**	**226**	**4,141**	**158**	**362**	**1,060**	**3,080**
%		97.9	18.4	18.5	5.2	95.8	3.7	8.4	24.5	71.2

Credit institutions grouped by registered authorised capital as of January 1, 2006

TABLE 14

Region	Under 3m rubles	3m to 10m rubles	10m to 30m rubles	30m to 60m rubles	60m to 150m rubles	150m to 300m rubles	300m rubles and over	Total
1	2	3	4	5	6	7	8	9
Russian Federation, total	**56**	**106**	**205**	**212**	**227**	**204**	**243**	**1,253**
Central Federal District	**18**	**40**	**79**	**118**	**128**	**141**	**190**	**714**
Belgorod Region	0	1	0	2	1	2	0	6
Bryansk Region	0	0	0	1	0	0	0	1
Vladimir Region	0	0	1	0	1	1	0	3
Voronezh Region	0	0	0	1	2	0	1	4
Ivanovo Region	1	0	1	2	1	0	0	5
Kaluga Region	0	0	0	1	2	1	1	5
Kostroma Region	1	1	1	1	0	0	1	5
Kursk Region	0	1	0	1	0	0	0	2
Lipetsk Region	0	0	0	0	1	1	0	2
Orel Region	0	0	0	2	0	0	0	2
Ryazan Region	0	1	0	3	0	0	0	4
Smolensk Region	0	2	0	1	0	0	1	4
Tambov Region	0	0	1	0	1	0	0	2
Tver Region	2	2	1	2	0	0	0	7
Tula Region	0	2	0	3	1	0	0	6
Yaroslavl Region	0	0	4	5	0	1	0	10
Moscow	14	29	68	90	116	132	182	631
Moscow Region	0	1	2	3	2	3	4	15
Moscow region (for the record)	*14*	*30*	*70*	*93*	*118*	*135*	*186*	*646*
North-Western Federal District	**8**	**10**	**22**	**15**	**13**	**6**	**10**	**84**
Republic of Karelia	0	0	0	0	1	0	0	1
Komi Republic	1	0	2	1	0	0	0	4
Arkhangelsk Region	1	2	0	1	0	0	0	4
of which: Nenets Autonomous Area	0	0	0	0	0	0	0	0
Vologda Region	0	0	4	1	2	0	1	8
Kaliningrad Region	1	0	3	5	1	1	1	12
Leningrad Region	0	0	2	0	1	0	0	3
Murmansk Region	1	0	1	0	0	2	0	4
Novgorod Region	0	1	0	0	0	1	0	2
Pskov Region	0	2	0	0	2	0	0	4
St Petersburg	4	5	10	7	6	2	8	42
Southern Federal District	**18**	**35**	**29**	**15**	**19**	**9**	**3**	**128**
Republic of Adygeya	1	4	0	0	0	0	0	5
Republic of Daghestan	9	12	10	2	2	1	0	36
Republic of Ingushetia	1	1	0	0	0	0	0	2
Kabardino-Balkar Republic	1	2	1	1	1	0	0	6
Republic of Kalmykia — Khalmg Tangch	0	0	0	0	2	0	0	2
Karachai-Cherkess Republic	1	1	3	0	0	0	0	5
Republic of North Ossetia — Alania	0	1	2	0	2	1	0	6
Chechen Republic	0	0	0	0	0	0	0	0
Krasnodar Territory	1	3	6	2	7	1	1	21
Stavropol Territory	1	6	1	2	0	0	0	10
Astrakhan Region	0	4	0	0	0	1	0	5
Volgograd Region	0	1	1	3	0	1	0	6
Rostov Region	3	0	5	5	5	4	2	24

END

Region	Under 3m rubles	3m to 10m rubles	10m to 30m rubles	30m to 60m rubles	60m to 150m rubles	150m to 300m rubles	300m rubles and over	Total
1	2	3	4	5	6	7	8	9
Volga Federal District	**6**	**5**	**24**	**26**	**38**	**22**	**25**	**146**
Republic of Bashkortostan	0	0	2	3	4	2	1	12
Republic of Marii El	0	0	1	0	0	0	0	1
Republic of Mordovia	0	0	1	0	2	1	0	4
Republic of Tatarstan	1	0	3	3	5	3	12	27
Udmurt Republic	0	1	2	2	2	0	2	9
Chuvash Republic	1	0	2	0	2	0	0	5
Kirov Region	0	0	1	0	1	0	1	3
Nizhny Novgorod Region	1	1	2	3	6	5	1	19
Orenburg Region	0	0	2	3	0	2	2	9
Penza Region	0	0	0	1	0	0	1	2
Perm Region	1	0	3	1	1	1	2	9
Samara Region	1	1	3	1	8	6	3	23
Saratov Region	0	2	1	5	7	2	0	17
Ulyanovsk Region	1	0	1	4	0	0	0	6
Ural Federal District	**2**	**4**	**13**	**15**	**8**	**13**	**12**	**67**
Kurgan Region	0	1	2	1	1	0	0	5
Sverdlovsk Region	2	1	4	5	2	8	5	27
Tyumen Region	0	1	4	7	3	3	5	23
of which: Khanty-Mansi Autonomous Area	0	1	0	5	0	2	4	12
Yamalo-Nenets Autonomous Area	0	0	3	1	0	1	0	5
Chelyabinsk Region	0	1	3	2	2	2	2	12
Siberian Federal District	**2**	**8**	**23**	**14**	**13**	**9**	**2**	**71**
Republic of Altai	0	0	4	1	0	0	0	5
Republic of Buryatiya	0	0	0	0	1	1	0	2
Republic of Tyva	0	1	0	1	0	0	0	2
Republic of Khakassia	0	1	1	0	0	1	0	3
Altai Territory	0	1	3	2	1	0	1	8
Krasnoyarsk Territory	0	0	2	1	2	1	0	6
of which: Taimyr Autonomous Area	0	0	0	0	0	0	0	0
Evenk Autonomous Area	0	0	0	0	0	0	0	0
Irkutsk Region	0	0	2	4	2	1	0	9
of which: Ust-Orda Buryat Autonmous Area	0	0	0	0	0	0	0	0
Kemerovo Region	0	1	2	1	2	2	0	8
Novosibirsk Region	2	2	5	0	3	1	1	14
Omsk Region	0	2	2	2	1	1	0	8
Tomsk Region	0	0	1	1	1	1	0	4
Chita Region	0	0	1	1	0	0	0	2
of which: Agin-Buryat Autonomous Area	0	0	0	0	0	0	0	0
Far Eastern Federal District	**2**	**4**	**15**	**9**	**8**	**4**	**1**	**43**
Republic of Sakha (Yakutia)	0	1	1	2	2	0	0	6
Primorskiy (Maritime) Territory	1	1	4	0	2	1	0	9
Khabarovsk Territory	0	1	2	1	1	0	1	6
Amur Region	0	1	2	0	1	1	0	5
Kamchatka Region	1	0	4	3	0	0	0	8
of which: Koryak Autonomous Area	0	0	1	0	0	0	0	1
Magadan Region	0	0	1	1	0	1	0	3
Sakhalin Region	0	0	1	2	2	1	0	6
Jewish Autonomous Region	0	0	0	0	0	0	0	0
Chukchee Autonomous Area	0	0	0	0	0	0	0	0

Quantitative characteristics of credit institutions

TABLE 15

Indicator	As of January 1, 2006	2005
No. of credit institutions registered by the Bank of Russia or the Registration Authority on the basis of the Bank of Russia decision	1,409	9
of which: non-bank credit institutions	53	3
No. of operating credit institutions licensed to conduct banking operations	1,253	8
of which non-bank credit institutions	48	3
No. of credit institutions established as a result of reorganisation	—	6
No. of credit institutions wound up as a result of acquisition	—	14
of which: credit institutions turned into branches of acquiring banks	—	8
No. of credit institutions turned from non-bank credit institutions into banks	—	1
No. of credit institutions turned from banks into non-bank credit institutions	—	0
No. of credit institutions which expanded the range of activities by obtaining additional licences	—	59
of which:		
to conduct banking operations with foreign exchange	—	14
to take household deposits in rubles or in rubles and in foreign currency	—	14
to conduct operations with precious metals	—	10
credit institutions which replaced permits by licences to conduct operations with precious metals	—	0
credit institutions obtaining a general licence	—	11
No. of credit institutions which had their licences replaced in 2005 due to restrictions being lifted	—	10
Dynamics on the types of licences held by credit institutions:	1,299	1,253
to take deposits	1,165	1,045
to conduct operations in foreign currency	839	827
general licences	311	301
to conduct operations with precious metals (licence or permit)	182	184
Change in aggregate authorised banking sector capital in 2005, million rubles	380,468	444,377
Change in grouping of credit institutions by registered authorised capital		
of which:		
under 3m rubles	73	56
3m to 10m rubles	133	106
10m to 30m rubles	232	205
30m to 60m rubles	225	212
60m to 150m rubles	211	227
150m to 300m rubles	191	204
300m rubles and over	234	243
Change in number of branches of credit institutions in 2005	3,238	3,295
of which: Sberbank branches	1,011	1,009
Change in number of internal divisions of credit institutions in 2005	27,670	29,634
of which:		
additional offices	9,068	11,368
cash offices	18,491	17,662
cash-credit offices	111	604

For notes

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